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United States

Vol. 1
1881

Circuit Court of Appeals

For the Ninth Circuit.

JACKSON C. SAIN, HETTIE SAIN, ED. RAY,
JOSEPH H. McDONALD, MISSOULA
COUNTY, TENNIE E. GREENOUGH,
CLARA PIDGE, W. T. BURNETT, GEORGE
CROMWELL, GLENN STICHT, G. W.
LEAPHART, JOSEPHINE YOUNGQUIST,
HARRY E. STETSON, et al.,

Appellants,

vs.

THE MONTANA POWER COMPANY,
a Corporation,

Appellee.

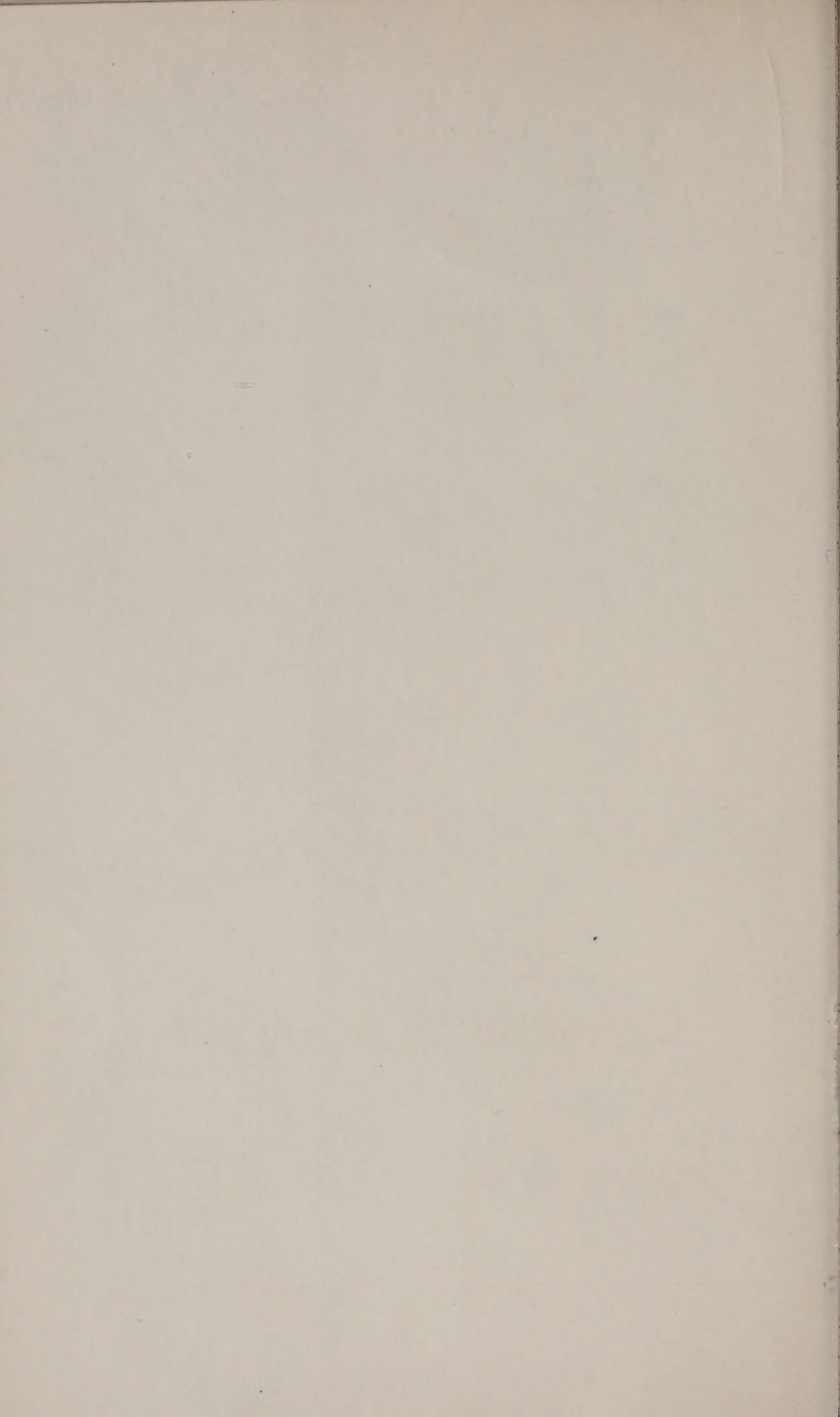
Transcript of Record

Upon Appeal from the District Court of the
United States for the District of Montana.

JUL 9 - 1934

PAUL P. O'BRIEN,

CLERK



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JOSEPH H. MURKIN, MISSOURI,
GEOFFREY, TERRY E. GREENBERG,
JAMES TERRY W. T. B. KURT GROVER,
GROWING, OLIVER, STOUT, G. W.
CLAMANT, JOSEPH, JOSEPH,
HARRY E. STETSON, et al.
Appellants

THE MONTANA POWER COMPANY,
a Corporation

Appellee

Transcript of Record

Upon Appeal from the District Court of the
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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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NAMES AND ADDRESSES OF SOLICITORS
OF RECORD.

Mr. S. P. WILSON,
of Deer Lodge, Montana, and
Mr. E. C. MULRONEY,
of Missoula, Montana,
Solicitors for Plaintiffs and Appellants.

Mr. W. L. MURPHY,
Mr. A. N. WHITLOCK,
Mr. WALTER L. POPE, and
Mr. JOHN E. CORETTE, Jr.,
All of Missoula Montana,
Solicitors for Defendant and Appellee. [1*]

In the District Court of the United States in and for
the District of Montana.

No. 1488.

JACKSON C. SAIN, et al.,
Plaintiffs,
vs.

THE MONTANA POWER COMPANY,
a corporation,
Defendant.

BE IT REMEMBERED, that on August 18th,
1933, Bill of Complaint was filed herein in the words
and figures following, to-wit: [2]

*Page numbering appearing at the foot of page of original certified
Transcript of Record.

In the United States District Court for the District
of Montana, Missoula Division

JACKSON C. SAIN, HETTIE SAIN, ED RAY,
JOSEPH H. McDONALD, MISSOULA
COUNTY, TENNIE E. GREENOUGH,
CLARA PIDGE, W. T. BURNETT, GEORGE
CROMWELL, GLEN STICHT, C. W.
LEAPHART, JOSEPHINE YOUNGQUIST,
HARRY E. STETSON, A. M. ROGERS, I. E.
PETERSON, H. E. STURM, MINNIE L.
McCANN, A. L. KAGLE, ISRAEL Q. ROB-
ERTS, WILLIAM J. JOHNSON, HORACE
A. GREEN, PEARL GREEN, W. D. SAT-
TERFIELD, MARGARET A. SATTER-
FIELD, E. F. ROTH, ELLEN R. WHITING,
L. A. WAGONER, CHARLES E. LUCAS,
CHARLES A. MARTINSON and FREDA
MARTINSON, co-partners doing business un-
der the firm name of MISSOULA ICE COM-
PANY, ORPHA MILLER TALBOTT, and
RUSSELL H. MILLER,

Plaintiffs,

vs.

THE MONTANA POWER COMPANY,
a Corporation,

Defendant.

COMPLAINT IN EQUITY. [3]

Come now the plaintiffs and complain of the de-
fendant and allege:

I.

Jurisdiction of this case arises and is conferred upon this Honorable Court by reason of the diversity of the citizenship of the parties hereto. The plaintiffs are, and each of them is, a citizen of the State of Montana, and a resident of Missoula County, Montana; the defendant is a corporation organized and existing under the laws of the State of New Jersey and is a citizen of the State of New Jersey. The matter in controversy in this action exceeds, exclusive of interest and costs, the sum and value of \$3000.00.

II.

That Missoula County, one of the plaintiffs herein, is a body politic and corporate, organized and existing under the laws of the State of Montana; that Missoula Ice Company, one of the plaintiffs herein, is a corporation, organized and existing under the laws of the State of Montana; that Montana Power Company, the defendant herein, is a corporation organized and existing under the laws of the State of New Jersey. [4]

III.

That Rattlesnake Creek, described in this complaint, is a stream of fresh and flowing water arising in the mountains north of Missoula in Missoula County, Montana, and flowing southwardly into Missoula River and is a tributary of said Missoula River and is situated in Missoula County, Montana.

IV.

That upon the 9th day of July, 1903, in the District Court of the Fourth Judicial District of the State of Montana, in and for the County of Missoula, in a cause then pending in said Court, wherein the Missoula Water Company was plaintiff and Charles E. Williams and others were defendants, being Cause No. 1953 of said court, a decree was duly given, made, rendered and entered, adjudicating the waters of said Rattlesnake Creek between appropriators and claimants to the use of the waters of said creek and determining the respective rights, priorities and amounts to the use of such waters among the said appropriators and users thereof, a copy of said decree and judgment being hereto attached, marked Exhibit A and made a part of this complaint to the same extent as if here set forth in full. By the judgment and decree aforesaid the rights, priorities, amounts of water and dates of appropriations of the waters of Rattlesnake Creek were fully adjudicated and determined and said Rattlesnake Creek became, and thereafter was, an adjudicated stream, as defined by Section 7128, Revised Codes of Montana, 1921, and that said judgment has not been reversed nor in any way modified nor set aside.

V.

That in said Cause No. 1953 the Court did make findings of fact, Finding of Fact No. 1 being as follows: [5]

“1. That the plaintiff by its predecessors in interest made an appropriation of 946 inches of the waters of Rattlesnake Creek, mentioned and described in the complaint herein, about April 1, 1866, by what is called the Mill ditch, for mechanical, power and other beneficial purposes, and that the same has been used by plaintiff and its predecessors in interest ever since, and that no part thereof has ever been abandoned.”

Finding of Fact No. 2 being:

“2. That the plaintiff by its predecessors in interest made an appropriation of 160 inches of the waters of said Rattlesnake Creek, November 16, 1868, by what is called the original Higgins ditch, and that no part of said appropriation has ever been abandoned.”

Finding of Fact No. 9 being:

“9. That the plaintiff, by its predecessors in interest, about May 1, 1881, enlarged the original Higgins ditch and extended it to other lands, increasing its capacity and use from 160 inches to 508 inches, thereby making an additional appropriation of the waters of said Rattlesnake Creek of 348 inches, of date May 1, 1881, and that no part thereof has ever been abandoned.”

Defendant claims ownership of the water rights and appropriations of the waters of Rattlesnake

Creek found, decreed and described in said Findings of Fact 1, 2 and 9, foregoing described, and defendant at the times alleged in this complaint has assumed possession of said water rights and appropriations of water and has diverted said waters from said Rattlesnake Creek and has made use thereof and claims the same.

VI.

That the water right and appropriation of water described in Finding of Fact No. 1, foregoing, was appropriated through what is called the Mill ditch out of said Rattlesnake Creek and at all times from the time of the appropriation thereof down to and long subsequent to the date of the judgment in said Cause No. 1953 said water so appropriated and found and decreed in said Cause No. 1953, was diverted out of Rattlesnake [6] Creek through said Mill ditch and was used for mechanical and power purposes along said Mill ditch and was not diverted elsewhere nor used for other purposes.

That the water right and appropriation of water described in Finding of Fact No. 2, foregoing, was appropriated through what is called the original Higgins Ditch out of said Rattlesnake Creek and at all times from the time of the appropriation thereof down to and long subsequent to the date of the judgment in said Cause No. 1953, said water so appropriated and found and decreed in said Cause No. 1953, was diverted out of Rattlesnake Creek through said original Higgins ditch and was used for irrigation upon agricultural lands along said original Higgins ditch and was not diverted elsewhere nor used for other purposes.

That the water right and appropriation of water described in Finding of Fact No. 9, foregoing, was appropriated through what is called the original Higgins ditch enlarged out of said Rattlesnake Creek and at all times from the time of the appropriation thereof down to and long subsequent to the date of the judgment in said Cause No. 1953, said water so appropriated and found and decreed in said Cause No. 1953, was diverted out of Rattlesnake Creek through said original Higgins ditch enlarged and was used for irrigation upon agricultural lands along said original Higgins ditch enlarged and was not diverted elsewhere nor used for other purposes.

Said Mill ditch taps said Rattlesnake Creek upon its right bank about a quarter of a mile above the mouth of Rattlesnake Creek. Said original Higgins ditch and as enlarged taps said Rattlesnake Creek upon its right bank at a point about *two above* the mouth of Rattlesnake Creek. [7]

VII.

Defendant Montana Power Company claims to be the successor in interest of the Missoula Water Company, who was the plaintiff in said Cause No. 1953, in the ownership of all waters, water rights and appropriations of water decreed to said The Missoula Water Company in Cause No. 1953, and defendant has taken, and now takes, possession of the waters of Rattlesnake Creek as the successor in title and in interest of The Missoula Water Company to the extent of the appropriations found in

said Findings of Fact 1, 2 and 9, foregoing described.

That subsequent to the 9th day of July, 1903, and long prior to the commencement of this section the defendant and its predecessors in interest did abandon the water rights hereinbefore described—that is to say, the water rights and appropriations of water found and decreed in said Findings of Fact 1, 2 and 9, and each, both and all said water rights and appropriations of water—and defendant and its predecessors have abandoned the right to the use of said water and all thereof.

VIII.

That subsequent to the date of said decree and prior to the wrongful acts of the defendant herein alleged, defendant and its grantors and predecessors in interest abandoned said Mill ditch and the appropriation of water made through said Mill ditch. Plaintiffs are informed and believe and therefore allege, that when defendant and its predecessors in interest abandoned said appropriation of water through said Mill ditch, to-wit: The water right described in Finding of Fact No. 1, foregoing, defendant and its grantors and predecessors in interest went upon said Rattlesnake Creek to a point higher up on said creek than the head of said Mill ditch, that is to say, to a point near the North line [8] of Township 13 North, Range 19 West, and there pretended and attempted to divert from Rattlesnake Creek 946 inches of water, claiming the same as the water right described in said Finding of Fact No. 1.

The water right and appropriation of water described in said Finding of Fact No. 1 for 946 inches of water was appropriated and was decreed to be taken from the water flowing in said creek at the head of said Mill ditch and not elsewhere.

That subsequent to the date of said decree and prior to the wrongful acts of the defendant herein alleged, defendant and its grantors and predecessors in interest abandoned said original Higgins ditch and the appropriation of water made through said original Higgins ditch. Plaintiffs are informed and believe, and therefore allege, that when defendant and its predecessors in interest abandoned said appropriation of water through said original Higgins ditch, to wit: the water right described in Finding of Fact No. 2, foregoing, defendant and its grantors and predecessors in interest went upon said Rattlesnake Creek to a point higher up on said creek than the head of said original Higgins ditch, that is to say, to a point near the North line of Township 13 North, Range 19 West, and there pretended and attempted to divert from Rattlesnake Creek 160 inches of water, claiming the same as the water right described in said Finding of Fact No. 2. The water right and appropriation of water described in said Finding of Fact No. 2 for 160 inches of water was appropriated and was decreed to be taken from the water flowing in said creek at the head of said original Higgins ditch and not elsewhere.

That subsequent to the date of said decree and prior to the wrongful acts of the defendant herein alleged, defendant [9] and its grantors and predecessors in interest abandoned said original Higgins ditch enlarged and the appropriation of water made through said original Higgins ditch enlarged. Plaintiffs are informed and believe, and therefore allege, that when defendant and its predecessors in interest abandoned said appropriation of water through said original Higgins ditch enlarged, to-wit: the water right described in Finding of Fact No. 9, foregoing, defendant and its grantors and predecessors in interest went upon said Rattlesnake Creek to a point higher up on said creek than the head of said original Higgins ditch enlarged, that is to say, to a point near the North line of Township 13 North, Range 19 West, and there pretended and attempted to divert from Rattlesnake Creek 348 inches of water, claiming the same as the water right described in said Finding of Fact No. 9. The water right and appropriation of water described in said Finding of fact No. 9 for 348 inches of water was appropriated and was decreed to be taken from the water flowing in said creek at the head of said original Higgins ditch enlarged and not elsewhere.

IX.

Plaintiffs Jackson C. Sain and Hettie Sain are the owners of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

Northwest Quarter of Southwest Quarter; East Half of East Half of Northwest Quarter of Southwest Quarter; six acres in the Northwest Quarter of the Southeast Quarter, all in Section Eleven, Township Thirteen North, Range Nineteen West.

The plaintiff Ed Ray is the owner of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit: [10]

Section Thirty-five (35) and the West Half of the West Half ($W\frac{1}{2}W\frac{1}{2}$) of Section Thirty-six (36), Township Fourteen (14) North, Range Nineteen (19) West.

The plaintiff Joseph H. McDonald is the owner of, in the possession of and entitled to the possession of the lands situated in Missoula County, Montana, and described in Exhibit "B" hereto attached and made a part of this complaint.

The plaintiff Missoula County is the owner of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

The Northeast Quarter of the Northwest Quarter ($NE\frac{1}{4} NW\frac{1}{4}$) of Section Fourteen (14), Township Thirteen (13) North, Range Nineteen (19) West.

The plaintiff Tennie E. Greenough is the owner of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

sion of the following described lands situated in the City of Missoula, Missoula County, Montana, to-wit:

All of Block Twenty-three (23), Lots One (1) to Eight (8) inclusive; and Lot Ten (10) of Block Twelve (12); Lots One (1) to Six (6), inclusive; and Lots Eighteen (18) to Twenty-four (24), inclusive, together with the vacated alley in Block Twenty-five (25); all in Park Addition, according to the plat thereof on file in the office of the County Clerk and Recorder of Missoula County, Montana.

Also, the North Half ($N\frac{1}{2}$) of Lot Sixteen (16); all of Lots Seventeen (17), Eighteen (18), Nineteen (19), Twenty (20), Twenty-one (21), and Twenty-two (22); and the North Half ($N\frac{1}{2}$) of Lot Twenty-three (23); in Block Nine (9) of said Park Addition.

Together with eight (8) acres in the Southwest corner of the Northeast Quarter of the Northwest Quarter ($NE\frac{1}{4}$ $NW\frac{1}{4}$) of Section Fourteen (14), Township Thirteen (13), North of Range Nineteen (19) West. [11]

The plaintiffs, Clara Pidge and W. T. Burnett, are the owners of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

Beginning at the Northwest corner of the Northwest Quarter of the Northeast Quarter of Sec. 14, T. 13 N., R. 19 W., and running thence South 30 feet to the Northwest corner

of the tract to be described and running thence East on a line posted with the North side line of said Forty 80 rods, more or less, to the east side line of said Forty; thence South along said East line 99 feet; thence West on a line parallel with the said North side line 80 rods, more or less, to the West side line of said Forty; thence North along said West side line 99 feet to the place of beginning, containing 3 acres, more or less.

Beginning at the Northwest corner of the Northwest Quarter of the Northeast Quarter of Sec. 14, T. 13 N., R. 19 W., M. M., running thence South along the West line of said Forty 8 rods to a point which is the Northwest corner of the tract to be described; thence East 80 rods, more or less, to the East line of said Forty, thence South along the East line of said Forty 10 rods; thence West 8 rods, more or less, to the West line of said Forty; thence North 10 rods to the place of beginning, containing 5 acres, more or less.

The plaintiffs, George Cromwell and Glen Sticht, are the owners of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

The Southeast Quarter of the Northeast Quarter and the South 526 feet of the Northeast Quarter of the Northeast Quarter of Sec. 14, T. 13 N., R. 19 W.

The plaintiff, C. W. Leaphart, is the owner of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

Beginning at the Southwest corner of the Southwest Quarter of the Northeast Quarter of Sec. 14, T. 13 N., R. 19 W., thence North 40 rods for a starting point; thence North 20 rods; thence East 80 rods, more or less; thence South 20 rods; thence West 80 rods, more or less, to the place of beginning, containing 10 acres, more or less.

The plaintiff, Josephine Youngquist, is the owner of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit: [12]

Lot 13 of the Cobban Camp Sites, according to the plat thereof on file in the office of the County Clerk and Recorder of Missoula County, Montana, containing 4 acres, more or less.

The plaintiff, Harry E. Stetson, is the owner of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

Lots 6, 10 and 11 of Cobban Camp Sites, according to the plat thereof on file in the office of the County Clerk and Recorder of Missoula County, Montana, containing 9 acres, more or less.

The plaintiff, A. M. Rogers, is the owner of, in the possession of and entitled to the possession of the following described lands situated in Missoula, County, Montana, to-wit:

Beginning at the Southwest corner of the Northwest Quarter of the Northeast Quarter of Sec. 14, T. 13 N., R. 19 W. of Montana Meridian and running thence North along the West line of said quarter 33 feet to a point which is the Southwest corner of the land to be described and running thence North along said line 165 feet; thence East in line parallel with the South line of said quarter 80 rods, more or less, to the East line of said quarter; thence South along said East line 165 feet; thence West 80 rods, more or less, to the place of beginning, containing 5 acres, more or less.

The plaintiff, I. E. Peterson, is the owner of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

The Northeast Quarter of Sec. 15, T. 13 N., R. 19 W., containing 157 acres, more or less.

The plaintiffs, H. E. Sturm and Minnie L. McCann, are the owners of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

Beginning at the Southwest corner of the Northwest Quarter of the Northeast Quarter

of Sec. 14, T. 13 N., R. 19 W., and running thence North 12 rods to a point which is the Southwest corner of the land to be described and running thence North 165 feet, thence East 80 rods, thence South 165 feet, thence West 80 rods, to place of beginning, containing 5 acres, more or less. [13]

The plaintiff, A. L. Kagle, is the owner of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

Commencing at the Southeast corner of the Northwest Quarter of the Northeast Quarter of Sec. 14, T. 13 N., R. 19 W., thence North along the East line of said quarter quarter section 363 feet to the Southeast corner of the tract to be described, thence West parallel with the South line of said quarter quarter section 80 rods, more or less, to the County Road, thence North 165 feet, thence East and parallel with the South line of said quarter quarter section 80 rods, more or less, to the East side line of said quarter quarter section, thence South 165 feet to the place of beginning, containing five acres, more or less.

The plaintiff, Israel Q. Roberts, is the owner of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

Beginning at the Southwest corner of the Northwest Quarter of the Southeast Quarter of Section 11, T. 13 N., R. 19 W., running thence North 2 rods to the Southwest corner of the tract to be described, thence East 40 rods, thence North 20 rods, thence West 40 rods, thence South 20 rods to the place of beginning, containing five acres, more or less.

The plaintiff, William J. Johnson, is the owner of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

Lots 1, 2, 3, 4, 5, 6, 7, 8, 9, 16, 17, 18, 19, 20, 21, 22, 23, and 24 of Block 30 of Park Addition to the City of Missoula, Montana, according to the official plat thereof on file in the office of the County Clerk and Recorder of Missoula County, Montana.

The plaintiffs, Horace A. Green and Pearl Green, are the owners of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

Lots 7, 8, 9, 10, 11, 12, 13, 14, 15, 16, 17, and 18 of Block 14 of Park Addition to the City of Missoula, Montana, according to the official plat thereof on file in the office of the County Clerk and Recorder of Missoula County, Montana.

[14]

The plaintiffs, W. D. Satterfield and Margaret A. Satterfield, are the owners of, in the possession of

and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

Lots 10, 11, 12, 13, 14 and 15 of Block 30 of Park Addition to the City of Missoula, Montana, according to the plat thereof on file in the office of the County Clerk and Recorder of Missoula County, Montana.

The plaintiffs, E. F. Roth and Ellen R. Whiting, are the owners of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

The Northwest Quarter of the Southeast Quarter of Section 14, T. 13 N., R. 19 W.

Also a tract, beginning at the Northwest corner of the Northwest Quarter of the Southeast Quarter of said Section 14, T. 13 N., R. 19 W., running thence North 330 feet, thence East 80 rods, thence South 330 feet, thence West 80 rods to the place of beginning, containing 50 acres, more or less.

The plaintiffs, L. A. Wagoner and Charles E. Lucas, are the owners of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

Beginning at the Northwest corner of the Southeast Quarter of Sec. 11, T. 13 N., R. 19 W., and thence South 30 feet to a point which is the Northwest corner of the tract herein de-

scribed, thence East 40 rods, thence South 32 rods, thence West 40 rods, thence North 32 rods to the place of beginning, containing 8 acres.

The plaintiffs, Charles A. Martinson and Freda Martinson, co-partners doing business under the firm name of Missoula Ice Company, are the owners of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

The East Half of the East Half of the Southwest Quarter of the Southwest Quarter and part of the West Half of the Southeast Quarter of the Southwest Quarter of Section 11, T. 13, N., R. 19 W., containing 26 acres [15] of land, together with an ice manufacturing plant for commercial purposes located thereon.

The plaintiffs, Orpha Miller Talbott and Russell W. Miller, are the owners of, in the possession of and entitled to the possession of the following described lands situated in Missoula County, Montana, to-wit:

A tract of land in the Northwest Quarter of the Northeast Quarter of Sec. 14, T. 13 N., R. 19 W., and particularly described as follows, to-wit: Beginning at the Southwest corner of the Northwest Quarter of the Northeast Quarter of said Section 14, and running thence North on the section line 528 feet to a point which is the Southwest corner of the tract to

be described, thence North along the section line 495 feet, thence on a line parallel with the south line of said quarter 80 rods, more or less, to the east side line of said quarter, thence south on said line 495 feet, thence west 80 rods, more or less, to the place of beginning, containing 15 acres.

Said lands of plaintiffs are all agricultural in character but dry and arid and incapable of producing crops without irrigation but will produce valuable crops when irrigated. [16]

X.

As an appurtenant to their land above described, plaintiffs J. C. Sain and Hattie Sain own and are entitled to the use and possession of the following described water rights out of Rattlesnake Creek, to-wit:

Right No. 18 in Cause No. 1953, decreed to William Neill, being 50 inches of the waters of said Rattlesnake Creek, as of August 29, 1890; that part of Right No. 21 in Cause No. 1953, decreed to William Neill, being 30 inches of the waters of Rattlesnake Creek, as of September 1, 1895; and that part of Right No. 21 in Cause No. 1953, decreed to E. J. Clements, being 6 inches of the waters of Rattlesnake Creek, as of September 1, 1895.

Said 50 inches of water of Rattlesnake Creek so decreed and established to William Neill by the decree in Cause No. 1953, were duly appropriated on August 29, 1890, by means of a dam constructed to

divert said water from Rattlesnake Creek and by means of a ditch constructed to convey said waters from said creek to and upon the lands above described of said plaintiffs and parts thereof for irrigation, domestic and other useful purposes and said waters and the whole thereof have been continuously used by said plaintiffs and their predecessors in interest upon said lands for such purposes since the date of the appropriation thereof and the whole of said waters is necessary for the proper irrigation of said lands.

Said 30 inches of water of Rattlesnake Creek so decreed and established to William Neill by the decree in Cause No. 1953, were duly appropriated on September 1, 1895, by means of a dam constructed to divert said water from Rattlesnake Creek and by means of a ditch constructed to convey said waters from said creek to and upon the lands above described of said [17] plaintiffs and parts thereof for irrigation, domestic and other useful purposes and said waters and the whole thereof have been continuously used by said plaintiffs and their predecessors in interest upon said lands for such purposes since the date of the appropriation thereof and the whole of said waters is necessary for the proper irrigation of said lands.

Said 6 inches of water of Rattlesnake Creek so decreed and established to E. J. Clements by the decree in Cause No. 1953, were duly appropriated on September 1, 1895, by means of a dam constructed to divert said water from Rattlesnake Creek and

by means of a ditch constructed to convey said waters from said creek to and upon the lands above described of said plaintiffs and parts thereof for irrigation, domestic and other useful purposes and said waters and the whole thereof have been continuously used by said plaintiffs and their predecessors in interest upon said lands for such purposes since the date of the appropriation thereof and the whole of said waters is necessary for the proper irrigation of said lands.

As an appurtenant to his land above described, Plaintiff Ed Ray owns and is entitled to the use and possession of the following described water rights out of Rattlesnake Creek, to-wit:

Right No. 17 in Cause No. 1953, decreed to Sebastian Effinger, being 100 inches of the waters of said Rattlesnake Creek, as of October 1, 1888.

Said 100 inches of water of Rattlesnake Creek so decreed and established to Sebastian Effinger by the decree in Cause No. 1953, were duly appropriated on October 1, 1888, by means of a dam constructed to divert said water from Rattlesnake Creek and by means of a ditch constructed to convey said waters from said creek to and upon the lands above described [18] of said plaintiff and parts thereof for irrigation, domestic and other useful purposes and said waters and the whole thereof have been continuously used by said plaintiff and his predecessors in interest upon said lands for such purposes since the date of the appropriation thereof and the whole of said waters is necessary for the proper irrigation of said lands.

As an appurtenant to his land, described in Exhibit "B" hereof, plaintiff J. H. McDonald owns and is entitled to the use and possession of the following described water rights out of Rattlesnake Creek, to-wit:

48 inches of right No. 5 of the waters of Rattlesnake Creek, decreed and established to Otto Quast, Jacob G. Ambrose and John A. Kapp, in Cause No. 1953, as of April 15, 1872; 40 inches of Right No. 10 of the waters of Rattlesnake Creek, in Cause No. 1953, decreed and established to H. C. Hollenbeck, as of August 28, 1882; 220.5 inches of Right No. 20 of the waters of Rattlesnake Creek, decreed and established to Otto Quast in Cause No. 1953, as of August 16, 1895; 56.8 inches of Right No. 21 of the waters of Rattlesnake Creek, decreed and established to H. C. Chattin, C. W. Chattin, B. F. Chattin and J. W. Chattin in Cause No. 1953, as of September 1, 1895.

Said 48 inches of water of Rattlesnake Creek so decreed and established to Otto Quast, Jacob G. Ambrose and John A. Kapp by the decree in Cause No. 1953, were duly appropriated on April 15, 1872, by means of a dam constructed to divert said water from Rattlesnake Creek and by means of a ditch constructed to convey said waters from said creek to and upon the lands of said plaintiff described in Exhibit "B" hereof, and parts thereof for irrigation, domestic and other useful purposes and said waters and the whole thereof have been continuously used by said plaintiff and his predecessors in inter-

est upon said lands for such purposes since [19] the date of the appropriation thereof and the whole of said waters is necessary for the proper irrigation of said lands.

Said 40 inches of water of Rattlesnake Creek so decreed and established to H. C. Hollenbeck by the decree in Cause No. 1953, were duly appropriated on August 28, 1882, by means of a dam constructed to divert said water from Rattlesnake Creek and by means of a ditch constructed to convey said waters from said creek to and upon the lands of the said plaintiff described in Exhibit "B" hereof, and parts thereof for irrigation, domestic and other useful purposes and said waters and the whole thereof have been continuously used by said plaintiff and his predecessors in interest upon said lands for such purposes since the date of the appropriation thereof and the whole of said waters is necessary for the proper irrigation of said lands.

Said 220.5 inches of water of Rattlesnake Creek so decreed and established to H. C. Chattin, C. W. Chattin, B. F. Chattin and J. W. Chattin by the decree in Cause No. 1953, were duly appropriated on September 1, 1895, by means of a dam constructed to divert said water from Rattlesnake Creek and by means of a ditch constructed to convey said waters from said creek to and upon the lands of said plaintiff described in Exhibit "B" hereof, and parts thereof for irrigation, domestic and other useful purposes and said waters and the whole

thereof have been continuously used by said plaintiff and his predecessors in interest upon said lands for such purposes since the date of the appropriation thereof and the whole of said waters is necessary for the proper irrigation of said lands.

As an appurtenant to its land above described, plaintiff Missoula County owns and is entitled to the use and possession of the following described water rights out of Rattlesnake Creek, to-wit: [20]

That part of Rights No. 10 and 16 in Cause No. 1953, decreed and established to Missoula County, being for 36 inches of the waters of Rattlesnake Creek, as of August 28, 1882.

Said 36 inches of water of Rattlesnake Creek so decreed and established to Missoula County by the decree in Cause No. 1953, were duly appropriated on August 28, 1882, by means of a dam constructed to divert said water from Rattlesnake Creek and by means of a ditch constructed to convey said waters from said creek to and upon the lands above described of said plaintiff and parts thereof for irrigation, domestic and other useful purposes and said waters, and the whole thereof, have been continuously used by said plaintiff upon said lands for such purposes since the date of the appropriation thereof and the whole of said waters is necessary for the proper irrigation of said lands.

As an appurtenant to each of their several lands above described, plaintiffs Tennie L. Greenough, Clara Pidge, W. T. Burnett, C. W. Leaphart, A. M.

Rogers, H. E. Sturm, Minnie L. McCann, A. L. Kagle, William J. Johnson, Horace A. Green, Pearl Green, E. F. Roth, Ellen R. Whiting, Orpha Miller Talbott and Russell H. Miller own and are entitled to the use and possession of the parts and portions of Rights No. 10 and 16 in Cause No. 1953, as follows:

Tennie L. Greenough	15.85 inches thereof;
Clara Pidge and W. T. Burnett	3.136 inches thereof;
C. W. Leaphart	7.056 inches thereof;
A. M. Rogers	4.332 inches thereof;
H. E. Sturm and	
Minnie L. McCann	3.95 inches thereof;
A. L. Kagle	3.563 inches thereof;
William J. Johnson	2.959 inches thereof;
Horace A. Green and	
Pearl Green	1.568 inches thereof;
E. F. Roth and	
Ellen R. Whiting	15.68 inches thereof;
Orpha Miller Talbott and	
Russell H. Miller	11.76 inches thereof.

Each and all said amounts of water were duly appropriated through [21] the Hollenbeck Ditch and the extension thereof upon the 28th day of August, 1882, by means of a dam constructed to divert said water from Rattlesnake Creek, and by means of a ditch constructed to convey said water from said creek to and upon the several separate lands of said respective plaintiffs, above described, and parts of said land for irrigation, domestic and other

useful purposes and said waters, and the whole thereof, have been used continuously by said respective plaintiffs upon said lands for such purposes since the date of the appropriation thereof, and the whole of said waters is necessary for the irrigation of said several tracts of land.

As an appurtenant to its land above described, plaintiffs George Cromwell and Glen Sticht own and are entitled to the use and possession of the following described water rights out of Rattlesnake Creek, to-wit:

That part of Right No. 20 in Cause No. 1953, decreed and established to Jeanette Francis Sticht, being for 5 inches of the waters of Rattlesnake Creek, as of August 16th, 1895.

Said 5 inches of water of Rattlesnake Creek so decreed and established to Jeanette Francis Sticht by the decree in Cause No. 1953 were duly appropriated on August 28th, 1882, by means of a dam constructed to divert said water from Rattlesnake Creek and by means of a ditch to convey said water from said creek to and upon the lands above described of said plaintiff, and parts thereof, for irrigation and other useful purposes and said water, and the whole thereof, have been continuously used by said plaintiffs upon said lands for such purposes since the date of the appropriation thereof and the whole of said water is necessary for the proper irrigation of said lands.

As an appurtenant to his land above described,

plain- [22] tiff owns and is entitled to the use and possession of the following described water right out of Rattlesnake Creek, to-wit:

5 inches of Right No. 20 in Cause No. 1953, decreed and established to Elmer Hughes as of August 16th, 1895, said 5 inches of water of Rattlesnake Creek so decreed and established to Elmer Hughes by the decree in Cause No. 1953 were duly appropriated on August 16th, 1895, by means of a dam constructed to divert said water from Rattlesnake Creek and by means of a ditch constructed to convey said water from said creek to and upon the lands above described of said plaintiff, and parts thereof, for irrigation, domestic and other useful purposes, and said waters, and the whole thereof, have been continuously used by said plaintiff upon said land for such purposes since the date of the appropriation thereof and the whole of said waters is necessary for the proper irrigation of said lands.

As an appurtenant to their land plaintiffs H. E. Sturm and Minnie L. McCann own and are entitled to the use and possession of 2½ inches out of right No. 20 in Cause No. 1953 decreed and established to Elmer Hughes as of date August 16th, 1895.

Said 2½ inches of the waters of Rattlesnake Creek so decreed and established to Elmer Hughes by the decree in Cause No. 1953 were duly appropriated on August 16th, 1895, by means of a dam constructed to divert said water from Rattlesnake Creek and by means of a ditch constructed to con-

vey said waters from said creek to and upon the lands above described of said plaintiffs, and parts thereof, for irrigation, domestic and other useful purposes and said waters, and the whole thereof, have been continuously used by said plaintiffs upon said lands for such purposes since the date of the appropriation thereof and the whole of said waters is necessary for the proper irrigation of said lands.

[23]

As an appurtenant to his land plaintiff A. L. Kagle owns and is entitled to the use and possession of 5 inches out of Right No. 20 in Cause No. 1953 decreed and established to Elmer Hughes as of date August 16th, 1895.

Said 5 inches of the waters of Rattlesnake Creek so decreed and established to Elmer Hughes by the decree in Cause No. 1953 were duly appropriated on August 16th, 1895, by means of a dam constructed to divert said water from Rattlesnake Creek and by means of a ditch constructed to convey said waters from said creek to and upon the lands above described of said plaintiff, and parts thereof, for irrigation, domestic and other useful purposes and said waters, and the whole thereof, have been continuously used by said plaintiff upon his lands for such purposes since the date of the appropriation thereof and the whole of said waters is necessary for the proper irrigation of said lands.

As an appurtenant to their land plaintiffs Orpha Miller Talbott and Russell H. Miller own and are

entitled to the use and possession of 15 inches out of right No. 20 in Cause No. 1953 decreed and established to Elmer Hughes as of date August 16th, 1895.

Said 15 inches of the waters of Rattlesnake Creek so decreed and established to Elmer Hughes by the decree in Cause No. 1953 were duly appropriated on August 16th, 1895, by means of a dam constructed to divert said water from Rattlesnake Creek and by means of a ditch constructed to convey said waters from said creek to and upon the lands above described of said plaintiffs, and parts thereof, for irrigation, domestic and other useful purposes, and said waters, and the whole thereof, have been continuously used by said plaintiffs upon said lands for such purposes since [24] the date of the appropriation thereof and the whole of said waters is necessary for the proper irrigation of said lands.

As an appurtenant to her land above described plaintiff Josephine Youngquist owns and is entitled to the use and possession of 5 inches of Right No. 22 in Cause No. 1953 decreed and established to W. R. Hamilton, H. E. Day and R. E. Brandt as of August 29th, 1898.

Said 5 inches of the waters of Rattlesnake Creek so decreed and established to Elmer Hughes by the decree in Cause No. 1953 were duly appropriated August 29th, 1898, by means of a dam constructed to divert said water from Rattlesnake Creek and by means of a ditch constructed to

convey said waters from said creek to and upon the lands above described of said plaintiff, and parts thereof, for irrigation, domestic and other useful purposes, and said waters, and the whole thereof, have been continuously used by said plaintiff upon said lands for such purposes since the date of the appropriation thereof and the whole of said waters is necessary for the proper irrigation of said lands.

As an appurtenant to his lands above described plaintiff I. E. Peterson owns and is entitled to the use and possession of 50 inches of right No. 22 in Cause No. 1953 decreed and established to W. R. Hamilton, as of August 29th, 1898.

Said 50 inches of the waters of Rattlesnake Creek so decreed and established to W. R. Hamilton by the decree in Cause No. 1953 were duly appropriated on August 29th, 1898 by means of a dam constructed to divert said water from Rattlesnake Creek and by means of a ditch constructed to convey said waters from said creek to and upon the lands above described of said plaintiff, and parts thereof, for irrigation, domestic and other useful purposes, and said waters, and the whole thereof, have been continuously [25] used by said plaintiff upon said lands for such purposes since the date of the appropriation thereof and the whole of said waters is necessary for the proper irrigation of said lands.

As an appurtenant to his land above described plaintiff Israel Q. Roberts owns and is entitled to the use and possession of 3 inches of Right No. 5 in

Cause No. 1953 decreed and established to Jacob G. Ambrose as of April 15th, 1872, and 14 inches of Right No. 21 decreed and established to Jacob G. Ambrose as of September 1st, 1895.

Said 17 inches of water of Rattlesnake Creek so decreed and established to Jacob G. Ambrose by the decree in Cause No. 1953 were duly appropriated, 3 inches thereof on April 15th, 1872, and 14 inches thereof on September 1st, 1895 by means of a dam constructed to divert said water from Rattlesnake Creek and by means of a ditch constructed to convey said waters from said creek to and upon the lands above described of said plaintiff, and parts thereof, for irrigation, domestic and other useful purposes, and said waters, and the whole thereof, have been continuously used by said plaintiff upon said lands for such purposes since the date of the appropriation thereof and the whole of said waters is necessary for the proper irrigation of said lands.

As an appurtenant to their lands above described plaintiffs L. A. Wagoner and Charles E. Lucas own and are entitled to the use and possession of 20½ inches of Right No. 21 in Cause No. 1953 decreed and established to R. M. Cobban, W. H. Raymond, C. E. Williams and William Neil as of date September 1st, 1895.

Said 20½ inches of the waters of Rattlesnake Creek so decreed and established to R. M. Cobban, W. H. Raymond, C. E. Williams and William Neil by the decree in Cause No. 1953 were duly appro-

priated on September 1st, 1895, by means of a dam construct- [26] ed to divert said water from Rattlesnake Creek and by means of a ditch constructed to convey said waters from said creek to and upon the lands above described of said plaintiffs, and parts thereof, for irrigation, domestic and other useful purposes, and said waters, and the whole thereof, have been continuously used by said plaintiffs upon said lands for such purposes since the date of the appropriation thereof and the whole of said waters is necessary for the proper irrigation of said lands.

As an appurtenant to its lands above described plaintiffs Charles A. Martinson and Freda Martinson, doing business under the firm name of Missoula Ice Company, own and are entitled to the use and possession of 150 inches of the waters of Rattlesnake Creek through the Hollenbeck Ditch as of August 1st, 1901; said 150 inches of water having been duly appropriated on August 1st, 1901, by means of a dam constructed to divert said water from said Rattlesnake Creek and by means of a ditch constructed to convey the same from said creek to and upon the lands above described for the purpose of ice manufacture and said water, and the whole thereof, have been continuously used by said plaintiffs for such purposes since the date of the appropriation thereof and the whole of said water is necessary for such uses. Said water is used only at a time after the expiration of the irrigation sea-

son in each year when the water is not required by any agricultural users of water from said Hollenbeck Ditch who are entitled to the use of the same and the right of the plaintiffs to such use of the water is to be limited to the purpose of ice manufacture and at a time of the year when the water is not required for irrigation by other users of water for irrigation through the Hollenbeck Ditch. [27]

XI.

The place of diversion of the water which each plaintiff is entitled to use is near the north line of Township 13, North Range 19 West.

XII.

Water more than sufficient to supply the 946 inches claimed by defendant and decreed to The Missoula Water Company from the water flowing in said stream at the head of said Mill ditch at all times herein mentioned did rise and has always risen in Rattlesnake Creek in the bed of said creek and in said Rattlesnake Creek basin below the points of diversion of plaintiffs and each and all of plaintiffs and above the head of said Mill ditch; notwithstanding the use by plaintiffs and each and all of plaintiffs of the water owned by them, and each of them, and which they, and each of them are entitled to use at all times herein mentioned, there always was and is sufficient water flowing in said creek at the head of said Mill ditch to supply

the water described in said Finding of Fact No. 1, and during all of the times mentioned in this complaint said 946 inches of water so appropriated and decreed for said Mill ditch flowed down said creek past the head of said Mill ditch and flowed to waste out of the mouth of said creek. During the seasons of 1931, 1932, and 1933, defendant and its predecessors in interest attempted to take 946 inches of water out of said creek near the north line of Township 13 North, Range 19 West, claiming the same to be the water right described in said Finding of Fact No. 1 and in so doing defendant did deprive plaintiffs and each of plaintiffs of water which plaintiffs and each of plaintiffs were entitled to use. That the pretended and attempted change in the point of diversion of the water described in said Finding of Fact No. 1 has resulted in injury to plaintiffs and each of [28] plaintiffs.

XIII.

Water more than sufficient to supply the 160 inches claimed by defendant and decreed to the Missoula Water Company from the water flowing in said stream at the head of said original Higgins ditch at all times herein mentioned did rise and has always risen in Rattlesnake Creek in the bed of said creek and in said Rattlesnake Creek basin below the points of diversion of plaintiffs and each and all of plaintiffs and above the head of said original Higgins ditch; notwithstanding the use by plaintiffs

and each and all of plaintiffs of the water owned by them, and each of them, and which they, and each of them, are entitled to use at all times herein mentioned, there always was and is sufficient water flowing in said creek at the head of said original Higgins ditch to supply the water described in said Finding of Fact No. 2, and during all of the times mentioned in this complaint said 160 inches of water so appropriated and decreed for said original Higgins ditch flowed down said creek past the head of said original Higgins ditch and flowed to waste out of the mouth of said creek. During the seasons of 1931, 1932 and 1933, defendant and its predecessors in interest attempted to take 160 inches of water out of said creek near the north line of Township 13 North, Range 19 West, claiming the same to be the water right described in said Finding of Fact No. 2 and in so doing defendant did deprive plaintiffs and each of plaintiffs of water which plaintiffs and each of plaintiffs were entitled to use. That the pretended and attempted change in the point of diversion of the water described in said Finding of Fact No. 2 has resulted in injury to plaintiffs and each of plaintiffs. [29]

XIV.

Water more than sufficient to supply the 348 inches claimed by defendant and decreed to The Missoula Water Company from the water flowing in said stream at the head of said original Hig-

gins ditch enlarged at all times herein mentioned did rise and has always risen in Rattlesnake Creek in the bed of said creek and in said Rattlesnake Creek basin below the points of diversion of plaintiffs and each and all of plaintiffs and above the head of said original Higgins ditch enlarged; notwithstanding the use by plaintiffs and each and all of plaintiffs of the water owned by them, and each of them, and which they, and each of them, are entitled to use at all times herein mentioned, there always was and is sufficient water flowing in said creek at the head of said original Higgins ditch enlarged to supply the water described in said Finding of Fact No. 9, and during all of the times mentioned in this complaint said 348 inches of water so appropriated and decreed for said original Higgins ditch enlarged flowed down said creek past the head of said original Higgins ditch enlarged and flowed to waste out of the mouth of said creek. During the seasons of 1931, 1932, and 1933, defendant and its predecessors in interest attempted to take 348 inches of water out of said creek near the north line of Township 13 North, Range 19 West, claiming the same to be the water right described in said Finding of Fact No. 9 and in so doing defendant did deprive plaintiffs and each of plaintiffs of water which plaintiffs and each of plaintiffs were entitled to use. That the pretended and attempted change in the point of diversion of the water described in said Finding of Fact No. 9 has resulted in injury to plaintiffs and each of plaintiffs.

XV.

That if defendant would divert the water decreed to The [30] Missoula Water Company and which defendant claims to have the right to use, at the head of the Mill ditch, original Higgins ditch, and original Higgins ditch enlarged, as hereinbefore described, then the water flowing in said creek near the north line of Township 13 North, Range 19 West, would all be available to supply the appropriations and rights of the plaintiffs, herein alleged, and defendant ought to supply its water right, if it has any such, at the heads of said Mill ditch, original Higgins ditch and original Higgins ditch enlarged; that by attempting to supply the rights decreed to The Missoula Water Company and which the defendant now claims the right to use at a point near the North line of Township 13 North, Range 19 West, defendant takes water from Rattlesnake Creek necessary to supply the rights of the plaintiffs, and all the plaintiffs, and deprives plaintiffs of water which they need and which they are entitled to use; at the same time defendant permits water flowing in said Rattlesnake Creek at the heads, respectively, of said Mill ditch, original Higgins ditch and original Higgins ditch enlarged, sufficient in quantity to supply its said rights, to flow to waste out of the mouth of said creek. During each of the irrigation seasons of 1931, 1932, and 1933, defendant diverted the water decreed to The Missoula Water Company and described in Findings of Fact numbered 1, 2 and 9, near the North Line of Township

13 North, Range 19 West, and did thereby exhaust the flow of Rattlesnake Creek and did prevent plaintiffs, and all of them, from using the water of said creek which they were entitled to use, to their irreparable damage and injury.

XVI.

Defendant, claiming to be the owner, claims the perpetual right to change the point of diversion of said waters so [31] described in Findings of Fact numbered 1, 2 and 9 of Cause No. 1953, and so decreed to The Missoula Water Company, to a point near the North line of Township 13 North, Range 19 West, and thereby intends to, and unless enjoined by this Court will, perpetually so divert the entire flow of Rattlesnake Creek to the irreparable damage and injury of plaintiffs, and each and all of the plaintiffs.

XVII.

By the attempted change of point of diversion aforesaid, defendant is depriving plaintiffs, and all of plaintiffs, of the waters which they own and which they, and each of them, need for the irrigation of their own agricultural crops, by reason whereof plaintiffs' agricultural crops are being injured and destroyed and defendant intends and threatens to continue said attempted change of point of diversion of said water perpetually and will so continue to divert said waters to the irreparable loss of all of the plaintiffs unless enjoined by this Court. The claim of defendant to the right to change said point

of diversion of water rights, which it claims, is without authority of law and is invalid.

XVIII.

The value of the use of the waters of Rattlesnake Creek to the plaintiffs of their water rights herein described exceeds \$25,000.00 and if defendant continues to make the change in the point of diversion of the waters, which defendant claims and as herein described, such acts of defendant will and do destroy the water rights of plaintiffs to their damage and injury in excess of \$25,000.00.

XIX.

The appropriations of the waters of Rattlesnake Creek of the plaintiffs and of each of the plaintiffs, herein described, [32] were accomplished and completed and many years prior in date to the pretended and attempted change of point of diversion of defendant and its predecessors in interest, from respectively the heads of the Mill ditch, original Higgins ditch and original Higgins ditch enlarged to a point near the North line of Township Thirteen North, Range 19 West; if defendant or its predecessors in interest ever acquired any right to divert any of the waters of Rattlesnake Creek at or near the last named point, such right of defendant is subsequent and junior to the rights of the plaintiffs, and each and all such rights, and is subject thereto, and defendant does not have the right to divert the waters of Rattlesnake Creek at or near the last named point at any time when the plaintiffs or any

of the plaintiffs have need for the waters of said creek.

XX.

That the acts and conduct of defendant herein alleged and claim of defendant herein alleged constitute and are a cloud upon plaintiffs' right and title to their several properties; and notwithstanding that defendant's said claims and acts are without authority of law, the same interfere with the right to his property of each plaintiff and with his enjoyment thereof and plaintiffs do not have, nor has any of the plaintiffs, any plain, speedy or adequate remedy at law.

WHEREFORE, plaintiffs demand judgment herein as follows:

1. That defendant be required to set forth its claims to the water rights and property herein described and that the same be decreed and adjudged to be junior and inferior to the rights of the plaintiffs and all of them and subject thereto.

2. That it be decreed by the Court that the attempted change of point of diversion of the water rights decreed to The Missoula [33] Water Company and described in Findings of Fact No. 1, 2 and 9, respectively, of the Decree in Cause No. 1953, has resulted in injury to the plaintiffs, and each of the plaintiffs, and that defendant be enjoined from continuing to make such change in point of diversion and be enjoined from claiming the right to change said point of diversion; that if defendant shall have any right to change the point of diver-

sion of said water rights or any thereof to a point near the North line of Township 13 North, Range 19 West, its right be decreed to be junior and inferior to the rights of plaintiffs and subject thereto.

3. That defendant be enjoined and restrained from interfering with plaintiffs' water rights herein described or the use by them or any of them of the waters of Rattlesnake Creek to which they or he may be entitled.

4. That plaintiffs have their costs herein incurred and such other and further relief as to the Court may seem equitable.

5. That a Writ of Subpoena issue herein, directed to the above named defendant, commanding it on a day certain to appear and answer this Bill of Complaint, but not under oath, answer under oath being hereby expressly waived.

S. P. WILSON,

Deer Lodge, Montana.

E. C. MULRONEY,

Missoula, Montana.

Attorneys for Plaintiffs.

United States of America,

State of Montana,

District of Montana.—ss.

Jackson C. Sain, being duly sworn, deposes and says: That he is one of the plaintiffs in the above entitled action and makes this verification for and on behalf of all the plaintiffs. Deponent has heard read the foregoing Bill of Complaint and knows the

contents thereof and deponent says that the same is true and correct of his own knowledge, except those allegations therein made upon information and belief and as to those, he believes the same to be true.

JACKSON C. SAIN.

Subscribed and sworn to before me this 16th day of August, 1933.

[Seal]

LILIAN C. WENZEL,

Notary Public for the State of Montana,
residing at Missoula, Montana.

My Commission expires Feb. 10, 1936. [34]

EXHIBIT "A"

In the District Court of the Fourth Judicial District
of the State of Montana, in and for
the County of Missoula

Cause No. 1933.

THE MISSOULA WATER COMPANY,
a Corporation,

Plaintiff,

vs.

CHARLES E. WILLIAMS, ET AL.,

Defendants.

Be it remembered that the above entitled cause came on regularly for trial on the 31st day of

March, 1902, and divers days thereafter, before the court, a trial by jury having been expressly waived by all the parties to the action appearing by their respective attorneys.

Evidence was introduced on the part of the plaintiff and on the part of the several defendants appearing herein, and also on the part of certain intervenors, and after the conclusion of the testimony the case was subsequently argued orally by counsel for the respective parties and briefs and written arguments were also submitted, and thereafter the cause was submitted to the court for decision; and the court having considered the pleadings of the several parties, the evidence and the arguments and briefs of counsel, and being advised in the premises, now makes the following findings of fact and conclusions of law, to-wit:

FINDINGS OF FACT

1. That the plaintiff by its predecessors in interest made an appropriation of 946 inches of the waters of Rattlesnake Creek, mentioned and described in the complaint herein, about April 1, 1866, by what is called the Mill Ditch, for mechanical, power and other beneficial purposes, and that the same has been used by plaintiff and its predecessors in interest ever since, [35] and that no part thereof has ever been abandoned.

2. That the plaintiff by its predecessors in interest made an appropriation of 160 inches of the waters of said Rattlesnake Creek November 16,

1868, by what is called the original Higgins ditch, and that no part of said appropriation has ever been abandoned.

3. That the plaintiff by its predecessors in interest made an appropriation of 13 and $\frac{1}{2}$ inches of the waters of said Rattlesnake Creek about April 1, 1871, by what is called the first water works or city flume or pipe, for the purpose of supplying the citizens of Missoula and vicinity with water for domestic, irrigation and other beneficial purposes, and that the same has been used continuously ever since, and that no part thereof has ever been abandoned.

4. That the plaintiff and the intervenor Philomene Fredline, as administratrix, of the estate of John A. Fredline, deceased, by their predecessors in interest, made an appropriation of 75 inches of the waters of Rattlesnake Creek about May 1, 1871, by what is called the Fredline ditch, and that the plaintiff is the owner of 65 inches thereof, and the said Philomene Fredline as such administratrix is the owner of 10 inches thereof.

6. That the intervenors Alvina Pelkey, Lovina Flagler and Gus Marotz by their predecessors in interest made an appropriation of 20 inches of the waters of said Rattlesnake Creek about May 1, 1875, by an enlargement of said Fredline ditch.

5. That the defendants Charles E. Williams, Jennie Williams, Otto Quast and Jacob G. Ambrose, and H. C. Chattin, John W. Chattin, Charles W. Chattin, Benjamin F. Chattin and John A.

Kapp, by their predecessors in interest, made an appropriation of 160 inches of the waters of the said Rattlesnake Creek about April 15th, 1872.

7. That the defendant Peter Federsohn, by his predecessors in interest, made an appropriation of 50 inches of the waters of the said Rattlesnake Creek about May 1, 1879, for power, [36] dairy and milk cooling purposes, by diverting the same from said creek and returning the same amount to the creek a short distance below the point of diversion, without using up or consuming any substantial part thereof.

8. That the plaintiff by its predecessors in interest about April 1, 1881, constructed a new flume or pipe for the water works or city flume, thereby increasing the capacity of said water works from 13 and $\frac{1}{2}$ inches to 60 inches, and thus made an additional appropriation of the waters of said Rattlesnake Creek, of said date, of $46\frac{1}{2}$ inches, for the same purpose as the original water works appropriation, and that no part thereof has ever been abandoned.

9. That the plaintiff, by its predecessors in interest, about May 1, 1881, enlarged the original Higgins ditch and extended it to other lands, increasing its capacity and use from 160 inches to 508 inches, thereby making an additional appropriation of the waters of said Rattlesnake Creek of 348 inches, of date May 1, 1881, and that no part thereof has ever been abandoned.

10. That the defendants H. C. Hollenbeck, Wallace P. Smith, Elmer Hughes, C. M. Owen, Emma

Schilling, Mary E. Nesmith, Mamie E. Murray, Ollie D. Mattison, Amanda Mattison, Refus Stryker, Alice M. Cobban, Lena Smith, A. E. Pound, H. C. Chattin, H. Hazleton, Adeline C. Biggs, Della T. Wright, Carrie B. Raymond, Beadie Moss, C. H. Moss, Effie M. Kilbourne, Thomas P. Street, A. B. Libby, W. A. Buswell, Mrs. E. H. Sherman, J. B. Frazier, J. E. Johnson, John White and Missoula County, by their predecessors in interest, August 28, 1882, made an appropriation of 145 inches of the waters of said Rattlesnake Creek, by what is called the Hollenbeck ditch conducting water to the Hollenbeck homestead.

11. That the defendant Peter Federsohn, by his predecessors in interest, made an appropriation of 130 inches of the waters of said Rattlesnake Creek on October 8, 1882.

12. That the defendant Missoula Lodge No. 13, Ancient Free and Accepted Masons, by its predecessors in interest made an appropriation of 30 inches of the waters of said Rattlesnake Creek [37] about June 1, 1884.

13. That the defendant Theodore Lachambre, by his predecessors in interest, made an appropriation of 20 inches of the waters of said Rattlesnake Creek, July 1, 1886.

14. That the plaintiff by its predecessors in interest about June 1, 1887, constructed a new flume and ditch for said water works, thereby increasing the capacity of said water works and the amount of water diverted and conducted thereby from 60 inches to 705 and $\frac{1}{2}$ inches, thereby making an

additional appropriation of the waters of said Rattlesnake Creek of 645 inches, of date June 1, 1887, for the same purposes as the two prior water works appropriations, and that no part thereof has even been abandoned.

15. That the defendant James S. Kemp made an appropriation of 100 inches of the waters of said Rattlesnake Creek June 1, 1888.

16. That the defendants H. C. Hollenbeck, Wallace P. Smith, Elmer Hughes, C. M. Owen, Emma Schilling, Mary F. Nesmith, Mamie E. Murray, Ollie D. Mattison, Amanda Mattison, Rufus Stryker, Alice M. Cobban, Lena Smith, A. E. Pount, H. C. Chattin, H. Hazleton, Adeline C. Biggs, Della T. Wright, Carrie B. Raymond, Beadie Moss, C. H. Moss, Effie M. Kilbourne, Thomas P. Street, A. B. Libby, W. A. Buswell, Mrs. E. H. Sherman, J. B. Frazier, J. E. Johnson, John White and Missoula County, by their predecessors in interest, made an additional appropriation of the waters of said Rattlesnake Creek to the appropriation mentioned in No. 10 of these Findings, to the extent of 50 inches, by an extension of the above mentioned Hollenbeck ditch to what is called the Daly pre-emption claim, on July 1, 1888.

17. That the defendant Sebastian Effinger made an appropriation of 100 inches of the waters of said Rattlesnake Creek about October 1, 1888.

18. That the defendant William Neill made an appropriation of 50 inches of the waters of said Rattlesnake Creek on August 29, 1890. [38]

19. That the defendant George Duncan made an appropriation of 50 inches of the waters of said Rattlesnake Creek, May 15, 1892.

20. That the defendants Charles E. Williams, Otto Quast, Elmer Hughes, Ollie D. Mattison, Mary F. Nesmith, Jeanette Stitch, John White and John G. Johnson, by their predecessors in interest, made an appropriation of 393 inches of the waters of said Rattlesnake Creek August 16, 1895.

21. That the defendants R. M. Cobban, W. H. Raymond, Charles E. Williams, William Neill, Jacob G. Ambrose, H. C. Chattin, C. W. Chattin, B. F. Chattin, J. W. Chattin, L. W. Barrett, E. J. Clements and John Capp, by their predecessors in interest made an appropriation of 341 inches of the waters of said Rattlesnake Creek on September 1, 1895.

22. That the defendants W. R. Hamilton, H. E. Day and R. E. Brandt made an appropriation of 75 inches of the waters of said Rattlesnake Creek August 29, 1898, and that the defendants Lucretia Worden, Lucina Worden Sterling, Henry O. Worden, Caroline Worden Dixon, Louise Worden Bradley, Frank L. Worden, Horace B. Worden and Ruth M. Worden also made an appropriation of 40 inches of the waters of said Rattlesnake Creek on said 29th day of August, 1898.

23. That the defendant A. E. Franklin made an appropriation of 100 inches of the waters of said Rattlesnake Creek on July 25, 1901.

CONCLUSIONS OF LAW

1. That the plaintiff is entitled to the use and enjoyment of 946 inches of the waters of Rattlesnake Creek, statutory measure, of date April 1, 1866.

2. That the plaintiff is entitled to the use and enjoyment of 160 inches of the waters of Rattlesnake Creek, statutory measure, of date November 16, 1868. [39]

3. That the plaintiff is entitled to the use and enjoyment of 13 and 1/2 inches of the waters of Rattlesnake Creek, statutory measure, of date April 1, 1871.

4. That the plaintiff is entitled to the use and enjoyment of 65 inches, and that the intervenor Philomene Fredline, as administratrix of the estate of John A. Fredline, deceased, is entitled to the use and enjoyment of 10 inches, of the waters of Rattlesnake Creek, statutory measure, both of date May 1, 1871.

6. That the intervenors Alvina Pelkey, Lovina Flagler and Gus Marotz are entitled to the use and enjoyment of 20 inches of the waters of Rattlesnake Creek, statutory measure, of date May 1, 1875.

5. That the defendants Charles E. Williams, Jennie Williams, Otto Quast, Jacob G. Ambrose, H. C. Chattin, John W. Chattin, Charles W. Chattin, Benjamin F. Chattin and John A. Kapp are entitled to the use and enjoyment of 160 inches of

the waters of Rattlesnake Creek, statutory measure, of date April 15, 1872.

7. That the defendant Peter Federsohn is entitled to the use and enjoyment of 50 inches of the waters of Rattlesnake Creek, of date May 1, 1879, for power, dairy and milk cooling purposes to be diverted and substantially the same amount to be returned to said creek a short distance below the point of diversion without substantial diminution or consumption.

8. That the plaintiff is entitled to the use and enjoyment of 46 and $\frac{1}{2}$ additional inches of the waters of said Rattlesnake Creek, statutory measure, of date April 1, 1881.

9. That the plaintiff is entitled to the use and enjoyment of 348 inches of the waters of Rattlesnake Creek, statutory measure, of date May 1, 1881. [40]

10. That the defendants H. C. Hollenbeck, Wallace P. Smith, Elmer Hughes, C. M. Owen, Emma Schilling, Mary F. Nesmith, Mamie E. Murray, Ollie D. Mattison, Amanda Mattison, Rufus Stryker, Alice M. Cobban, Lena Smith, A. E. Pound, H. C. Chattin, H. Hazelton, Adeline C. Biggs, Della T. Wright, Carrie B. Raymond, Beadle Moss, C. H. Moss, Effie M. Kilbourne, Thomas P. Street, A. B. Libby, W. A. Buswell, Mrs. E. H. Sherman, J. B. Frazier, J. E. Johnson, John White and Missoula County, are entitled to the use and enjoyment of 145 inches of the waters of Rattlesnake Creek, statutory measure, of date August 28, 1882.

11. That the defendant Peter Federsohn is entitled to the use and enjoyment of 130 inches of the waters of Rattlesnake Creek, statutory measure, of date October 8, 1882.

12. That the defendant Missoula Lodge No. 13, Ancient Free and Accepted Masons, is entitled to the use and enjoyment of 30 inches of the waters of Rattlesnake Creek, statutory measure, of date June 1, 1884.

13. That the defendant Theodore Lachambre is entitled to the use and enjoyment of 20 inches of the waters of Rattlesnake Creek, statutory measure, of date July 1, 1886.

14. That the plaintiff is entitled to the use and enjoyment of 645 inches of the waters of Rattlesnake Creek, statutory measure, of date June 1, 1887.

15. That the defendant James S. Kemp is entitled to the use and enjoyment of 100 inches of the waters of Rattlesnake Creek, statutory measure, of date June 1, 1888.

16. That the defendants H. C. Hollenbeck, Wallace P. Smith, Elmer Hughes, C. M. Owen, Emma Schilling, Mary F. Nesmith, Mamie E. Murray, Ollie D. Mattison, Amanda Mattison, Rufus Stryker, Alice M. Cobban, Lena Smith, A. E. Pound, [41] H. C. Chattin, H. Hazleton, Adeline C. Biggs, Della T. Wright, Carrie B. Raymond, Beadie Moss, C. H. Moss, Effie M. Kilbourne, Thomas P. Street, A. B. Libby, W. A. Buswell, Mrs. E. H. Sherman, J. B. Frazier, J. E. Johnson, John White and Missoula County, are entitled to the use and enjoyment of an additional appropriation of 50 inches

of the waters of Rattlesnake Creek, statutory measure, of date July 1, 1888.

17. That the defendant Sebastian Effinger is entitled to the use and enjoyment of 100 inches of the waters of Rattlesnake Creek, of date October 1, 1888.

18. That the defendant William Neill is entitled to the use and enjoyment of 50 inches of the waters of Rattlesnake Creek, of date August 29, 1890.

19. That the defendant George Duncan is entitled to the use and enjoyment of 50 inches of the waters of Rattlesnake Creek, statutory measure, of date May 15, 1892.

20. That the defendant Charles E. Williams, Otto Quast, Elmer Hughes, Ollie D. Mattison, Mary F. Nesmith, Jeanette Stich, John White and John G. Johnson are entitled to the use and enjoyment of 393 inches of the waters of Rattlesnake Creek, statutory measure, of date August 16, 1895.

21. That the defendants R. M. Cobban, W. H. Raymond, Charles E. Williams, William Neill, Jacob G. Ambrose, H. C. Chattin, C. W. Chattin, B. F. Chattin, J. W. Chattin, L. W. Barrett, E. J. Clements and John Capp are entitled to the use and enjoyment of 341 inches of the waters of Rattlesnake Creek, statutory measure, of date September 1, 1895.

22. That the defendants W. R. Hamilton, H. E. Day and R. E. Brandt are entitled to the use and enjoyment of 75 inches of the waters of Rattlesnake Creek, and that the defendants Lucretia Worden, Lucina Worden Sterling, Henry O. Worden, [42]

Caroline Worden Dixon, Louise Worden Bradley, Frank L. Worden, Horace B. Worden and Ruth M. Worden are entitled to the use and enjoyment of 40 inches of the waters of Rattlesnake Creek, statutory measure, and both of date August 29, 1898.

23. That the defendants A. E. Franklin is entitled to the use and enjoyment of 100 inches of the waters of Rattlesnake Creek, statutory measure, of date July 25, 1901.

THE PREMISES CONSIDERED, it is ordered, adjudged and decreed, and this doth order, adjudge and decree that the rights and priorities of the several parties to this action to the use of the said waters of Rattlesnake Creek be and the same are hereby fixed according to the amounts and dates as above ascertained in the findings of fact and conclusions of law, which findings of fact and conclusions of law are hereby referred to and made a part of this decree.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that the several parties to this action, and their successors in interest, and their agents, servants and employes, and all persons acting by, through or under them, be and they are hereby perpetually enjoined from in any manner interfering with the rights of each of the other parties as herein established.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that each of the parties to this action be and he is hereby required to construct a measuring box and headgate at the head of his ditch

so that the water that each is entitled to under the terms and provisions of this decree can at any time be measured thereby.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that the water hereby decreed to each of the parties is to be measured in the manner provided by the statutes of Montana. [43]

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that none of the parties hereto shall recover costs, but that each of said parties shall bear the costs incident to establishing his rights.

Done in open court this 9th day of July, 1903.

FREDERICK C. WEBSTER,

Judge.

(Filed: July 9th, 1903. [44])

EXHIBIT "B"

All that portion of land in Lot Four (4) and the Southeast Quarter of the Northwest Quarter, (SE $\frac{1}{4}$ NW $\frac{1}{4}$), of Section One (1), Township Thirteen (13), North of Range Nineteen (19), West of the Montana Meridian, lying south of the "Hogback" or ridge dividing the waters that flow north into Woods Gulch, and in Lot Four (4) consisting of about Fifteen (15) Acres, more or less, and in the Southeast Quarter of the Northwest Quarter (SE $\frac{1}{4}$ NW $\frac{1}{4}$) about Twenty-five (25) Acres, more or less, or a total of about Forty (40) Acres, more or less; said Hogback or ridge crosses the west line of said Section One (1) about 800 feet north of the South-

west corner of said Lot Four (4) and runs in a southeasterly direction to about the southeast corner of said Lot Four (4) and, continuing southeasterly in the same direction generally across the said southeast quarter of the northwest quarter ($SE\frac{1}{4}$ $NW\frac{1}{4}$) of Section One (1).

The Southwest Quarter ($SW\frac{1}{4}$), the Southeast Quarter ($SE\frac{1}{4}$), and the Southwest Quarter of the Northwest Quarter ($SW\frac{1}{4}$ $NW\frac{1}{2}$), of Section One (1), Township Thirteen (13), North of Range Nineteen (19) West, containing Three Hundred Sixty (360) Acres, more or less.

The South Half of the Southeast Quarter of the Northwest Quarter of the Southeast Quarter ($S\frac{1}{2}$ $SE\frac{1}{4}$ $NW\frac{1}{4}$ $SE\frac{1}{4}$) of Section Eleven (11), Township Thirteen (13), North of Range Nineteen (19) West, containing Five (5) Acres, more or less.

The North Half of the Southwest Quarter of the Southeast Quarter ($N\frac{1}{2}$ $SW\frac{1}{4}$ $SE\frac{1}{4}$), and the Southeast Quarter of the Southwest Quarter of the Southeast Quarter ($SE\frac{1}{4}$ $SW\frac{1}{4}$ $SE\frac{1}{4}$), of Section Eleven (11), Township Thirteen (13), North of Range Nineteen (19) West, containing Thirty (30) Acres, more or less.

The Southeast Quarter of the Southeast Quarter ($SE\frac{1}{4}$ $SE\frac{1}{4}$) of Section Eleven (11), Township Thirteen (13), North of Range Nineteen (19) West, containing Forty (40) Acres, more or less.
containing FortC

The North Half of the Northeast Quarter ($N\frac{1}{2}$ $NE\frac{1}{4}$), the North Half of the Northwest Quarter

(N $\frac{1}{2}$ NW $\frac{1}{4}$), The Southwest Quarter (SW $\frac{1}{4}$), and the Southeast Quarter (SE $\frac{1}{4}$), of Section Twelve (12), Township Thirteen (13), North of Range Nineteen (19) West, containing Four Hundred Eighty (480) Acres, more or less.

The Northwest Quarter (NW $\frac{1}{4}$), the Northwest Quarter of the Southwest Quarter (NW $\frac{1}{4}$ SW $\frac{1}{4}$), and the West Half of the Southwest Quarter (W $\frac{1}{2}$ SW $\frac{1}{4}$), of Section Thirteen (13), Township Thirteen (13), North of Range Nineteen (19) West, containing Two Hundred Twenty (220) Acres, more or less.

Beginning at the northeast corner of the Northeast quarter (NE Cor. of NE $\frac{1}{4}$), of Section Fourteen (14), Township Thirteen (13), North of Range Nineteen (19) West, and running thence south on the east side line of said quarter a distance of 40 rods to the northeast [45] corner of the tract to be conveyed and running thence west on a line parallel with the north side line of said quarter a distance of 80 rods, more or less, to the west line of the northeast quarter of said Section Fourteen (14); thence running south on the west line of said forty acre tract a distance of six (6) rods; thence running east 80 rods, more or less, to the east line of said quarter; thence running north six (6) rods to the place of beginning, containing three (3) acres, more or less.

Also beginning at the Southwest corner of the Northeast Quarter of the Northeast Quarter (NE $\frac{1}{4}$

NE $\frac{1}{4}$) of Section Fourteen (14), Township Thirteen (13), North of Range Nineteen (19) West, and running thence north along sub-division line a distance of 625 feet to a point which is the southwest corner of the tract to be conveyed, and running thence north along said sub-division line a distance of 660 feet; thence running east parallel with the north side line of said quarter a distance of 80 rods, more or less, to the east side line of said quarter; thence running south 660 feet; thence running west 80 rods, more or less, to the Southwest corner of the tract to be conveyed, and containing Twenty (20) Acres, more or less.

The Southeast Quarter of the Northeast Quarter (SE $\frac{1}{4}$ NE $\frac{1}{4}$), the East Half of the Southeast Quarter (E $\frac{1}{2}$ SE $\frac{1}{4}$), and Lot One (1), of Section Two (2), Township Thirteen (13), North of Range Nineteen (19) West, containing One Hundred Forty-eight and $\frac{23}{100}$ (148.23) Acres, more or less.

The total acreage of the foregoing descriptions being about Thirteen Hundred and Fifty-six (1356) Acres.

[Endorsed]: Complaint filed Aug. 18, 1933. [46]

Thereafter, on September 6, 1933, Motion to Dismiss was duly filed herein, in the words and figures following, to-wit: [47]

[Title of Court and Cause.]

MOTION TO DISMISS.

Comes now the defendant in the above entitled action and moves the court to dismiss said action upon the ground and for the reason:

I.

That the same does not state facts sufficient to constitute a valid cause of action in equity against the defendant.

W. L. MURPHY,
A. N. WHITLOCK,
JOHN E. CORETTE, Jr.

Missoula, Montana,
Attorneys for Defendant.

Service of the foregoing motion accepted and receipt of copy acknowledged this 5th day of September, 1933.

S. P. WILSON, &
E. C. MULRONEY,
Attorneys for Plaintiffs.

[Endorsed]: Filed Sept. 6, 1933. [48]

Thereafter, on October 18, 1933, the Motion to Dismiss herein was by the court denied, the record thereof being in the words and figures following, to-wit:

No. 1488, Jackson C. Sain et al. vs. Montana Power Co.

By agreement of counsel for the respective parties, Mr. E. C. Mulronev appearing for plaintiffs and Mr. W. L. Murphy for defendant, the motion to dismiss herein was submitted without argument; whereupon court ordered that said motion be denied, defendant granted until Oct. 21, 1933, to answer, and case set for trial Oct. 25, 1933, at 9:30 A. M.

Entered in open court October 18, 1933.

C. R. GARLOW,

Clerk. [49]

Thereafter, on October 18, 1933, Answer was duly filed herein, in the words and figures following, to wit: [50]

[Title of Court and Cause.]

ANSWER

Comes now the defendant in the above entitled action and for an answer to the complaint of the plaintiffs filed therein admits, denies and alleges as follows:

I.

Admits that the plaintiffs are citizens and residents of Missoula County, Montana, and admits that the defendant is a [51] corporation organized and existing under the laws of the State of New Jersey. Denies that the amount in controversy exceeds \$3000.00.

II.

Admits that Missoula County is a body politic and corporate, existing under the laws of Montana. Admits that Missoula Ice Company is a Montana corporation, and that defendant is a New Jersey corporation.

III.

Admits that Rattlesnake Creek, referred to in the complaint, is a stream of fresh water rising in the mountains north of Missoula, Missoula County, Montana, and flowing in a southerly direction to the Missoula River in said county.

IV.

Admits that on the 26th day of July, 1904, in the District Court of the Fourth Judicial District of the State of Montana, in and for the County of Missoula, in Cause No. 1953, wherein Missoula Water Company was plaintiff, and Charles E. Williams, and others, were defendants, a decree was duly given, made and entered, adjudicating the waters of said Rattlesnake Creek and determining the respective rights and priorities with reference thereto, and admits that "Exhibit A" made a part of the plaintiffs' complaint is a copy of said decree. In making this admission the defendant assumes that the date of the decree intended to be alleged was July 9, 1903, instead of July 9, 1930, as written in the copy of the complaint served upon this defendant.

V.

Admits that the court, among other findings, made Findings of Fact Nos. 1, 2, and 9, set out in Par-

agraph V of the complaint, and in this connection alleges that the court [52] made other findings awarding various other rights to Missoula Water Company, plaintiff in that case, all of which are set out in the copy of the decree attached to the plaintiffs' complaint. Admits that the defendant claims ownership of the rights described in said findings 1, 2 and 9, and alleges in that regard that it is the successor in interest of said Missoula Water Company and as such is the owner of said rights and all other rights awarded to Missoula Water Company under said decree, and admits that it has assumed possession of said rights and has to the extent necessary to meet its needs and to the extent authorized by said decree, diverted and used the waters of Rattlesnake Creek.

VI.

Admits that the right described in Finding of Fact No. 1 was appropriated through a ditch known as the Mill Ditch, but denies that at the time of and subsequent to the said decree in Cause No. 1953, the water so appropriated was diverted through said Mill ditch, and alleges that Cause No. 1953 was tried upon the assumption by the parties thereto that the water adjudicated to the plaintiff for use for furnishing the city and inhabitants of the city of Missoula, including said right, would and could be diverted at a single point, namely, the present point of diversion from Rattlesnake Creek, and that at the time the decree in said cause was made and entered the necessary works for such

diversion had been constructed and the water required to serve the city and inhabitants of the City of Missoula was being diverted at said point and has since been so diverted, and while a portion of the water so adjudicated to the said Missoula Water Company was for a time after said decree diverted through the said Mill ditch, such [53] diversion was thereafter discontinued more than twenty years prior to the bringing of this action, and at the date of said decree, and at all times since, said right to the extent necessary for furnishing the city of Missoula and its inhabitants was and is diverted at the present point of diversion, all as set forth hereinafter in defendant's first separate defense.

Admits that the right described in Finding of Fact No. 2 was appropriated through what is called the original Higgins ditch out of said Rattlesnake Creek, but denies that at the time of and subsequent to the said decree in Cause No. 1953, the water so appropriated was diverted through said Higgins ditch, and alleges that Cause No. 1953 was tried upon the assumption by the parties thereto that the water adjudicated to the plaintiff for use for furnishing the city and inhabitants of the city of Missoula, including said right, would and could be diverted at a single point, namely, the present point of diversion from Rattlesnake Creek, and that at the time the decree in said cause was made and entered the necessary works for such diversion had been constructed and the water required to serve the city and inhabitants of the City of Missoula was being diverted at said point and has since been

so diverted, and while a portion of the water so adjudicated to the said Missoula Water Company was for a time after said decree diverted through the said Higgins ditch, such diversion was thereafter discontinued more than twenty years prior to the bringing of this action, and at the date of said decree, and at all times since, said right to the extent necessary for furnishing the city of Missoula and its inhabitants, was and is diverted at the present point of diversion, all as set forth in defendant's first separate defense. [54]

Admits that the water right described in Finding of Fact No. 9, was appropriated through what is called the Higgins Ditch Enlarged, out of Rattlesnake Creek, but denies that at the time of and subsequent to the said decree in Cause No. 1953, the water so appropriated was diverted through said Higgins ditch enlarged, and alleges that Cause No. 1953 was tried upon the assumption by the parties thereto that the water adjudicated to the plaintiff for use for furnishing the city and inhabitants of the city of Missoula, including said right, would and could be diverted at a single point, namely, the present point of diversion from Rattlesnake Creek, and that at the time the decree in said cause was made and entered the necessary works for such diversion had been constructed and the water required to serve the city and inhabitants of the city of Missoula was being diverted at said point and has since been so diverted, and while a portion of the water so adjudicated to the said Missoula Water Company was for a time after said decree diverted

through the said Higgins ditch enlarged, such diversion was thereafter discontinued more than twenty years prior to the bringing of this action, and at the date of said decree, and at all times since, said right to the extent necessary for furnishing the city of Missoula and its inhabitants, was and is diverted at the present point of diversion, all as set forth hereinafter in defendant's first separate defense.

Admits that Mill ditch, referred to, tapped the Rattlesnake Creek about a quarter of a mile above its mouth, and admits that the said Higgins ditch tapped said Creek at a point about two miles above the mouth thereof.

Save as in this paragraph admitted the defendant [55] denies the allegations of Paragraph VI of said complaint.

VII.

Admits that the defendant claims to be, and alleges that it is the successor in interest of The Missoula Water Company, the plaintiff in Cause No. 1953, in the ownership of the water, water rights, and appropriations decreed to said The Missoula Water Company in said cause, and admits that it now takes possession of and uses the water as adjudicated in said rights and the other rights of The Missoula Water Company as fixed in said decree to the extent necessary to satisfy its needs. The defendant denies that it or any of its predecessors did subsequent to the 9th day of July, 1903, or at any other time, or at all, abandon any of the water rights described in the plaintiffs' complaint,

or any other water rights awarded to it or its predecessors by the decree in said cause, or to which it or its predecessors in interest were entitled from Rattlesnake Creek.

Save as in this paragraph admitted the defendant denies the allegations of Paragraph VII of said complaint.

VIII.

The defendant denies that there have been any wrongful acts on its part as alleged in Paragraph VIII of the complaint, and denies that the defendant or its grantors or predecessors in interest, or any of them, at any time abandoned said Mill ditch or any appropriation of water made through the same, or any other appropriation of water made from Rattlesnake Creek, and denies that defendant or any of its predecessors at any time abandoned any part of the water right described in Finding of Fact No. 1, but does allege that at the time of the decree in said cause, and since said time, it and [56] its predecessors have diverted said water to the extent required at the present location of defendant's dam and works, which is at a point higher up said Rattlesnake Creek than the head of said Mill ditch. That the extent of such diversion and the facts relating thereto, are fully set forth hereinafter in the defendant's first affirmative defense. Denies that the water right described in Finding of Fact No. 1 was appropriated or decreed to be taken at the head of said Mill ditch and not elsewhere.

The defendant denies that there have been any wrongful acts on its part as alleged in Paragraph VIII of the complaint, and denies that the defend-

ant or its grantors or predecessors in interest, or any of them, at any time abandoned said Higgins ditch or any appropriation of water made through the same, or any other appropriation of water made from Rattlesnake Creek, and denies that defendant or any of its predecessors at any time abandoned any part of the water right described in Finding of Fact No. 2, but does allege that at the time of the decree in said cause, and since said time, it and its predecessors have diverted said water to the extent required at the present location of defendant's dam and works, which is at a point higher up said Rattlesnake Creek than the head of said Higgins ditch. That the extent of such diversion and the facts relating thereto, are fully set forth hereinafter in the defendant's first affirmative defense. Denies that the water right described in Finding of Fact No. 2 was appropriated or decreed to be taken at the head of said Higgins ditch and not elsewhere.

The defendant denies that there have been any wrongful acts on its part as alleged in Paragraph VIII of the [57] complaint, and denies that the defendant or its grantors or predecessors in interest, or any of them, at any time abandoned said Higgins ditch enlarged, or any appropriation of water made through the same, or any other appropriation of water made from Rattlesnake Creek, and denies that defendant or any of its predecessors at any time abandoned any part of the water right described as Finding of Fact No. 9, but does allege that at the time of the decree in said cause, and since said time,

it and its predecessors have diverted said water to the extent required at the present location of defendant's dam and works, which is at a point higher up said Rattlesnake Creek than the head of said Higgins ditch enlarged. That the extent of such diversion and the facts relating thereto, are fully set forth hereinafter in the defendant's first affirmative defense. Denies that the water right described in Finding of Fact No. 9 was appropriated or decreed to be taken at the head of said Higgins ditch enlarged and not elsewhere.

Save as in this paragraph admitted the defendant denies the allegations of Paragraph VIII of said complaint.

IX.

Admits that the plaintiffs Jackson C. Sain and Hettie Sain are the owners of and in the possession of the lands described as belonging to them in Paragraph IX of the plaintiffs' complaint.

Denies that plaintiff Ed Ray is the owner of the land described as belonging to him in said paragraph, and alleges on information and belief that the ownership of said property is in Charles B. Effinger.

Denies that plaintiff Joseph H. McDonald is the owner of any of the lands described in "Exhibit B" attached to [58] the complaint, and alleges upon information and belief that the Federal Land Bank of Spokane is such owner.

Admits that plaintiff Missoula County is the owner of and in possession of the land described in Paragraph IX as belonging to it, with the exception of 8.09 acres thereof, which defendant is

informed and believes and therefore alleges has been conveyed by it to Tennie E. Greenough.

Admits that the plaintiff Tennie E. Greenough is the owner of and in possession of the lands described in Paragraph IX as belonging to her.

Admits that plaintiffs Clara Pidge and W. T. Burnett are the owners of and in possession of the lands described in Paragraph IX as belonging to them.

Denies that plaintiffs George Cromwell and Glen Sticht are the owners of the land described in Paragraph IX as belonging to them, and allege on information and belief that the title to said property is in Glen Sticht alone.

Admits that plaintiff C. W. Leaphart is the owner of and in possession of the land described in Paragraph IX as belonging to him.

Admits that plaintiff Josephine Youngquist is the owner of and in possession of the land described in Paragraph IX as belonging to her.

Admits that plaintiff Harry E. Stetson is the owner of and in possession of the land described in Paragraph IX as belonging to him, except his ownership is denied as to the south 38 feet of Lot 6 of Cobban Camp Sites.

Admits that plaintiff A. M. Rogers is the owner of and in possession of the lands described in Paragraph IX as belonging to him. [59]

Admits that plaintiff I. E. Peterson is the owner of and in possession of the lands described in Paragraph IX as belonging to him.

Denies that plaintiffs H. E. Sturm and Minnie L. McCann are the owners of or entitled to possession of the lands described in Paragraph IX as belonging to them.

Admits that plaintiff A. L. Kagle is the owner of and in possession of the lands described in Paragraph IX as belonging to him.

Admits that plaintiff Israel Q. Roberts is the owner of and in possession of the lands described in Paragraph IX as belonging to him.

Admits that plaintiff William J. Johnson is the owner of and in possession of the lands described in Paragraph IX as belonging to him.

As to the lands described in Paragraph IX as belonging to Horace A. Green and Pearl Green, the defendant denies the allegations with reference thereto, and alleges upon information and belief that the title is in Pearl Green alone.

Admits that plaintiffs W. D. Satterfield and Margaret A. Satterfield are the owners of and in possession of the lands described in Paragraph IX as belonging to them.

Admits that plaintiff Ellen R. Whiting is the owner of the lands described in Paragraph IX as belonging to E. F. Roth and Ellen R. Whiting, and denies the allegation in said paragraph as to the ownership of Roth.

Admits that plaintiff Charles E. Lucas is the owner of the lands described in Paragraph IX as belonging to L. A. Wagoner and Charles E. Lucas, and denies the allegations of said paragraph as to the ownership of Wagoner. [60]

Admits that plaintiffs Charles A. Martinson and Freda Martinson, doing business under the firm name of Missoula Ict Company, are the owners of and in possession of the lands described in Paragraph IX as belonging to them.

Admit that plaintiffs Orpha Miller Talbott and Russell W. Miller are the owners of and in possession of the lands described in Paragraph IX as belonging to them.

Admits that the lands of the plaintiffs are in each instance to some extent agricultural in character, requiring water for irrigation, but denies that all of said lands are of such character.

X.

Answering Paragraph X of plaintiffs' complaint the defendant admits that Missoula County is the owner of a portion of rights No. 10 and 16, as adjudicated by said decree in Cause No. 1953, and admits upon information and belief that the extent of said right is 36 inches. As to all of the other plaintiffs named in said paragraph defendant denies that they, or any of them, are entitled to the rights alleged, and denies all the allegations of said paragraph with reference thereto.

XI.

The defendant denies that the place of diversion of water by the several plaintiffs is near the north line of Township 13 North of Range 19 West.

XII.

The defendant denies that at the times mentioned in the plaintiffs' complaint, or at any time, water sufficient to supply 946 inches, or any other amount, at the head of said Mill ditch rose in Rattlesnake Creek below the points of diversion of plaintiffs, and denies that there was during said times sufficient water flowing in said creek at the head of the Mill ditch to supply the water described in Finding of Fact [61] No. 1 if the rights claimed by the plaintiffs were used, and denies that 946 inches of the water of said stream, or any other portion of the right described in Finding of Fact No. 1 flowed to waste out of the mouth of said creek at any time when water was required along said stream for beneficial purposes. Admits that during the seasons 1931, 1932 and 1933, the defendant diverted from Rattlesnake Creek at its present point of intake located a little less than one-half mile south of the north line of Township 13 North of Range 19 West, such water as was required by it to supply the needs of the city of Missoula and its inhabitants, and admits that the defendant claimed, and still claims, the right to make such diversion to the extent needed from the right described in said Finding of Fact No. 1. That the extent and character of said use is fully set forth hereinafter in the defendant's first affirmative defense. Defendant denies that it did at said times, or at any time, deprive the plaintiffs, or any of them, of any water to the use of which they or any of them were entitled. Denies that the diver-

sion of said water at said point has resulted in any injury whatsoever to the plaintiffs, or any of them.

The defendant denies all allegations of Paragraph XII not specifically admitted or denied in this paragraph.

XIII.

The defendant denies that at the times mentioned in the plaintiffs' complaint, or at any time, water sufficient to supply 160 inches, or any other amount, at the head of said Higgins ditch rose in Rattlesnake Creek below the points of diversion of plaintiffs, and denies that there was during said time sufficient water flowing in said creek at the head of the Higgins ditch to supply the water described in Finding of Fact [62] No. 2 if the rights claimed by the plaintiffs were used, and denies that 160 inches of the water of said stream, or any other portion of the right described in Finding of Fact No. 2 flowed to waste out of the mouth of said creek at any time when water was required along said stream for beneficial purposes. Admits that during the seasons 1931, 1932 and 1933, the defendant diverted from Rattlesnake Creek at its present point of intake located a little less than one-half mile south of the north line of Township 13 North of Range 19 West, such water as was required by it to supply the needs of the city of Missoula and its inhabitants, and admits that the defendant claimed, and still claims, the right to make such diversion to the extent needed from the right described in said Finding of Fact No. 2. That the extent and character of said

use is fully set forth hereinafter in the defendant's first affirmative defense. Defendant denies that it did at said times, or at any time, deprive the plaintiffs, or any of them, of any water to the use of which they or any of them were entitled. Denies that the diversion of said water at said point has resulted in any injury whatsoever to the plaintiffs, or any of them.

The defendant denies all allegations of Paragraph XIII, not specifically admitted or denied in this paragraph.

XIV.

The defendant denies that at the times mentioned in the plaintiffs' complaint, or at any time, water sufficient to supply 348 inches, or any other amount, at the head of said Higgins ditch enlarged rose in Rattlesnake Creek below the points of diversion of plaintiffs, and denies that there was during said time sufficient water flowing in said creek at the head of [63] the Higgins ditch enlarged to supply the water described in Finding of Fact No. 9 if the rights claimed by the plaintiffs were used, and denies that 348 inches of the water of said stream, or any other portion of the right described in Finding of Fact No. 9 flowed to waste out of the mouth of said creek at any time when water was required along said stream for beneficial purposes. Admits that during the seasons 1931, 1932, and 1933, the defendant diverted from Rattlesnake Creek at its present point of intake located a little less than one-half mile south of the north line of Township

13 North of Range 19 West, such water as was required by it to supply the needs of the city of Missoula and its inhabitants, and admits that the defendant claimed, and still claims, the right to make such diversion to the extent needed from the right described in said Finding of Fact No. 9. That the extent and character of said use is fully set forth hereinafter in the defendant's first affirmative defense. Defendant denies that it did at said times, or at any time, deprive the plaintiffs, or any of them, of any water to the use of which they or any of them were entitled. Denies that the diversion of said water at said point has resulted in any injury whatsoever to the plaintiffs, or any of them.

The defendant denies all allegations of Paragraph XIV not specifically admitted or denied in this paragraph.

XV.

The defendant denies that if it diverted its requirements of water at the heads of the said Mill ditch and Higgins ditch there would be any more water available in Rattlesnake Creek at any point for the plaintiffs, or any of them, and denies that the defendant by diverting water at the point where it now diverts [64] it about one-half mile south of the north line of Township 13 North of Range 19 West, deprives plaintiffs, or any of them, of any water from Rattlesnake Creek to the use of which they are entitled, and denies that by said diversion it causes any water to go to waste which could otherwise be utilized. Defendant admits that during the irrigation season of 1931, 1932, and 1933, it

diverted the water necessary to supply the requirements of the city of Missoula and its inhabitants at the point above located, but denies that by so doing it deprived the plaintiffs, or any of them, of water from Rattlesnake Creek to the use of which they were entitled, or that it did them any damage or injury.

Save as in this paragraph specifically admitted or denied, the defendant denies all other allegations of Paragraph XV of plaintiffs' complaint.

XVI.

The defendant admits that it claims to be, and alleges that it is the owner of the rights described in Findings of Fact numbered 1, 2 and 9 in Cause No. 1953, decreed to the Missoula Water Company, the defendant being the successor in interest of said company, and admits that it claims the right to divert said water within the limits of its adjudicated rights and to the extent necessary to supply its requirements at a point on Rattlesnake Creek a little less than one-half mile south of the north line of Township 13 North of Range 19 West, but denies that by so doing it does or will cause any damage or injury to the plaintiffs, or any of them. In this connection defendant alleges that the said point of diversion was in fact being used at the time of the entry of decree in Cause No. 1953, in which said rights are adjudicated. [65]

XVII.

The defendant denies that by its diversion at the point referred to it deprived the plaintiffs, or any of

them, of any water of Rattlesnake Creek to which they are entitled, or that it causes any damage or injury to the plaintiffs, or any of them. Denies that its right to divert water at said point is without authority of law or invalid, and denies all other allegations of Paragraph XVII. Defendant further alleges that the point of diversion to which the plaintiff refers in Paragraph XVII as a changed point is in fact the point at which water was being diverted at the time the decree in said Cause No. 1953 was entered.

XVIII.

Defendant denies that the value of the water rights of Rattlesnake Creek belonging to plaintiffs is \$25,000.00, and denies that the defendant by the diversion of the waters of Rattlesnake Creek has at any time, or now does in any way damage or injure the plaintiffs, or any of them.

XIX.

Defendant denies that the appropriations of the plaintiffs, or any of them, from Rattlesnake Creek antedate the right of the defendant to divert water at its present point of diversion, and allege in this regard that such rights as plaintiffs may have to the use of said water were adjudicated by the terms of the decree in Cause No. 1953, which is attached to the plaintiffs' complaint, and that the rights of plaintiffs' predecessors were adjudicated at the same time and in the same way, and that at the time of said decree water was being diverted by de-

fendant's predecessor at its present point of diversion, and that said cause was tried and said [66] decree entered upon the assumption that the rights of the defendant and its predecessors could and would be diverted at said point. The defendant denies that its right to divert water from Rattlesnake Creek at its present point is subsequent or junior to the rights of the plaintiffs, or any of them, and denies that it has no right to divert water at said point when plaintiffs have need of water, and denies all other allegations of Paragraph XIX, and alleges on the contrary that the defendant's rights and priorities are the same as adjudicated to the plaintiff, the Missoula Water Company, in Cause No. 1953, except as to other rights since acquired by the defendant and its predecessors not material to this controversy.

XX.

Denies that any act or conduct of the defendant referred to in the plaintiffs' complaint constitutes or is a cloud on any right or claimed right of any of the plaintiffs, and denies that any such act or conduct has interfered with or does interfere with the plaintiffs, or any of them, in any way. Denies that there is any wrong, damage or injury resulting to any of the plaintiffs.

XXI.

Except as herein specifically admitted or denied, the defendant denies all of the allegations of the plaintiffs' complaint. [67]

FOR A FURTHER ANSWER AND FIRST
SEPARATE DEFENSE TO THE PLAINTIFFS'
COMPLAINT THE DEFENDANT ALLEGES:

I.

That it is and since long prior to its acquisition of the water rights and water system hereinafter referred to, has been a corporation organized and existing under and by virtue of the laws of the state of New Jersey, authorized to engage in, and actually engaging in business in the state of Montana. That it is the successor in interest of The Missoula Water Company, a corporation, and as such has succeeded to all the property, rights and interest of that company in so far as the same consist of the right to use the water from Rattlesnake Creek and the distribution system and works used for supplying water to the City of Missoula and its inhabitants. That the defendant and its predecessors is and were public utilities at all times herein referred to, engaged in the business of providing a suitable water supply for domestic, irrigation and other beneficial purposes to the city of Missoula, Montana, and its inhabitants, and for fire protection in said city, and having the right of eminent domain. That in the furnishing of such water supply this defendant is the owner, and its predecessors in interest were the owners of the distribution system used for the distribution of water in Missoula and the reservoir, pipes, dam, and other works for the diversion, purification and distribution for consumption by members of the public of water in said city.

II.

That prior to the year 1903 the said The Missoula Water Company, predecessor in interest of this defendant, instituted as plaintiff a certain action in the District Court [68] of the Fourth Judicial District of the State of Montana, in and for the County of Missoula, the same being Cause No. 1953, and that C. E. Williams and many others were the defendants therein. That said action was brought for the purpose of adjudicating the waters of Rattlesnake Creek, being the stream referred to in the plaintiffs' complaint, and that decree was duly made and given in said action on the 26th day of July, 1904, copy of which decree is attached to the plaintiffs' complaint and made a part of it. That by the terms of said decree the plaintiff in said cause was awarded right No. 1 out of said stream, entitling it to the use of 946 inches as of April 1, 1866; right No. 2, entitling it to the use of 160 inches as of November 16, 1868; right No. 3, entitling it to the use of 13½ inches as of April 1, 1871; a part of right No. 4, entitling it to the use of 65 inches as of May 1, 1871; a part of right No. 8, entitling it to the use of 46½ inches as of April 1, 1881; right No. 9, entitling it to the use of 348 inches as of May 1, 1881; right No. 14, entitling it to the use of 645 inches as of June 1, 1887. That since the entry of said decree the defendant's predecessors have acquired by purchase a portion of right No. 5 under said decree, giving the right to use 115 inches of water as of April 15, 1872; right No. 11, giving the right to the

use of 130 inches of water as of October 8, 1882; right No. 19, giving the right to the use of 50 inches of water as of May 15, 1892; a portion of right No. 20, giving it the right to the use of 65 inches as of August 16, 1895; and a part of right No. 21, giving it the right to the use of 142 inches as of September 1, 1895. That the defendant as successor in interest of its predecessors is now the owner of all of said rights to the use of water from [69] Rattlesnake Creek, including those adjudicated to The Missoula Water Company, as above set forth, and also those since acquired by the defendant's predecessors in interest.

III.

That the purpose for which the water was appropriated by and decreed to the said plaintiff in said cause was to furnish a suitable water supply to the city of Missoula, Montana, a municipal corporation, for fire protection and other proper city purposes, and likewise to furnish a suitable water supply to the inhabitants of said city for domestic, irrigation and other purposes, and that said water rights at said time, and since, were and have been the only source of supply for said city and its inhabitants. That the plaintiff in its amended complaint in said action prayed for the right to take from said Rattlesnake Creek at one place all of the water to which it was found to be entitled, and that all of the plaintiffs in this action or their predecessors in interest were parties to said action, namely, Cause No. 1953, and that no objection was made in any of the answers

to the granting of such prayer. That said cause was tried upon the assumption that the said plaintiff could divert the rights adjudicated to it at one point, and that no controversy existed between the parties as to that question. That when the decree in said cause was signed and filed a dam had been constructed in Rattlesnake Creek at a point approximately one-half mile south of the north line of Township 13 North of Range 19 West, for the purpose of diverting the water from said stream which might be adjudicated to the said plaintiff, and that there had likewise been constructed a pipe line leading from the said dam to a reservoir, which was likewise constructed, and that all of said [70] works for the diversion, purification and distribution of said water to the city of Missoula and its inhabitants had been completed and the water necessary for such purpose was at the time of said decree, and prior thereto, being diverted at said point by defendant's predecessor in interest, and furnished to the city of Missoula and its inhabitants, and it has since been so furnished continuously. That the amount required for such purpose at said time was less than the amount adjudicated under rights No. 1, No. 2 and No. 9, by said decree. That prior to the construction of the dam and works herein referred to, the right designated in said decree as right No. 1, was partially diverted through what was known as the Mill ditch, which was located down stream from the point where said dam was located, and that the rights designated as No. 2 and No. 9 were partially

diverted through what is known as the Higgins ditch, likewise located down stream from said point, and that prior to the construction of said dam the total amount of water embraced in rights No. 1, No. 2 and No. 9, was diverted through said ditches and through other ditches, flumes and pipes and utilized at and beyond the city of Missoula, and none of it was returned to Rattlesnake Creek, and none of it was available after its use by the appropriators for use by any of the plaintiffs or their predecessors in interest. That after the construction of said dam, as herein alleged, the rights referred to in Findings No. 1, No. 2, and No. 9, and the other rights awarded to defendant's predecessors by said decree, were to the extent necessary to furnish the city of Missoula and its inhabitants diverted at the point where said dam was located, and that by consolidating said rights [71] and diverting them at said point and carrying the water from said dam through a pipe to the reservoir and distribution system, the amount of water required to satisfy the needs of defendant and its predecessors was much less than the amount required to satisfy rights No. 1, 2 and 9, when the same were taken out through the Mill and Higgins ditches, and other ditches, flumes and pipes and that the burden on the stream resulting from such diversion at one point greatly decreased the amount of water required to be diverted by the defendant and its predecessors to satisfy their needs, and greatly increased the amount of water available from said stream for use by the plaintiffs and their predeces-

sors herein, and that such condition has continued from said time to the present, and still continues.

IV.

That for some time after the diversion at said dam, as herein alleged, a portion of the said right No. 1 continued to be diverted through said Mill ditch, and a portion of rights No. 2 and 9 continued to be diverted through said Higgins ditch, but such uses were gradually discontinued and were entirely discontinued more than twenty years prior to the bringing of this action, and the use of said rights, and all rights to which the defendant and its predecessors were and are entitled to the extent that the same have been necessary to satisfy the requirements of the city of Missoula and its inhabitants, have been diverted at the present point of diversion at said dam and used for said purposes. That in establishing a single point of diversion at said dam the defendant and its predecessors did not intend to, and did not abandon any of the rights to which they were entitled, but established such point of diversion for the purpose of conserving the waters of said [72] stream and more efficiently serving the city of Missoula, and not otherwise.

V.

That the rights to the waters of said Rattlesnake Creek were adjudicated by said decree in said Cause No. 1953, and such adjudication was made in the light of the existing fact that the rights of

the plaintiff in said cause were at the time of decree being diverted and used at a single point of diversion, which is the present point of diversion. That since said time the plaintiffs and their predecessors in interest have acquiesced in the diversion of the water required by the defendant and its predecessors at said point of diversion and the waters of said stream have since that date been distributed annually by water commissioners appointed by the court having jurisdiction in the premises to distribute said water and the rights of defendant and its predecessors have been distributed at said point. The defendant alleges that its right to divert water is superior and prior to the rights of the plaintiffs and their predecessors to the extent fixed and determined in said decree in said Cause No. 1953, and that the water diverted by defendant and its predecessors has at no time exceeded but has at all times been less than the amount as to which priority was given to defendant's predecessor in said decree, and that the method and place of diversion followed by defendant and its predecessors, as herein alleged, has been and is to the advantage and benefit of the plaintiffs and their predecessors in interest, and that the plaintiffs have no just ground of complaint. [73]

FOR A FURTHER ANSWER AND SECOND SEPARATE DEFENSE THE DEFENDANT ALLEGES:

I.

That it is a New Jersey corporation authorized to do business in Montana, and a public utility owning and operating a dam, reservoir and purification

system, pipe lines and distribution system for the furnishing of water to the city of Missoula and its inhabitants, and having the power of eminent domain. That its predecessors before it were likewise public utilities, owners of the same system, and engaged in operating it.

II.

That the defendant is the successor in interest of The Missoula Water Company, a corporation, which was the plaintiff in that certain cause No. 1953, in the District Court of the Fourth Judicial District of the State of Montana, in and for the county of Missoula, which action was brought to adjudicate the waters of Rattlesnake Creek referred to in the plaintiff's complaint, and that final decree in said cause was made and entered on the 26th day of July, 1904, a copy thereof being attached to the plaintiffs' complaint, which decree by its terms adjudges The Missoula Water Company, defendant's predecessor, to be entitled to certain rights from said stream including the rights designated by the plaintiffs as No. 1, No. 2, and No. 9, as set forth in said decree.

III.

That at the time of said decree the rights of defendant's said predecessor in interest, including said rights last referred to, to the extent necessary to supply the city of Missoula and its inhabitants, were being diverted at a point on said stream about one-half mile south of the north line of [74] Township 13 North of Range 19 West, Montana Meridian, the same being the point of location of defendant's diversion dam, and that said water has since prior

to the date of said decree been continuously diverted at said point and used for said purpose.

IV.

That while the defendant claims that its rights to the waters of said stream and the rights of its predecessors thereto have been and are superior and prior to the rights of the plaintiffs, or any of them, or any of their predecessors, and that their right to divert their requirements up to the amounts fixed in said decree at the said present point of diversion has at all times existed, and still exists, the defendant alleges that such diversion by it and its predecessors in interest at said point, and such use, has been for a period of more than thirty years continuous, open, notorious, exclusive, uninterrupted, under claim of right, and adverse to the plaintiffs and their predecessors and all other persons, and the defendant alleges that by reason of these facts, if not otherwise, defendant's right to the use of the waters of said stream from said point of diversion in so far as necessary to satisfy the requirements of the defendant in furnishing the city of Missoula and its inhabitants is superior to the right of any of the plaintiffs or their predecessors.

[75]

FOR A FURTHER ANSWER AND THIRD SEPARATE DEFENSE, THE DEFENDANT ALLEGES:

I.

That it is a New Jersey corporation authorized to do business in Montana, and a public utility

owning and operating a dam, reservoir and purification system, pipe lines and distribution system for the furnishing of water to the city of Missoula and its inhabitants, and having the power of eminent domain. That its predecessors before it were likewise public utilities, owners of the same system, and engaged in operating it.

II.

That the defendant is the successor in interest of The Missoula Water Company, a corporation, which was the plaintiff in that certain cause No. 1953, in the District Court of the Fourth Judicial District of the State of Montana, in and for the county of Missoula, which action was brought to adjudicate the waters of Rattlesnake Creek referred to in the plaintiffs' complaint, and that final decree in said cause was made and entered on the 26th day of July, 1904, a copy thereof being attached to the plaintiffs' complaint, which decree by its terms adjudges The Missoula Water Company, defendant's predecessor, to be entitled to certain rights from said stream, including the rights designated by the plaintiffs as No. 1, No. 2, and No. 9, as set forth in said decree.

III.

That at the time of said decree the rights of defendant's said predecessor in interest, including said rights last referred to, to the extent necessary to supply the city of Missoula and its inhabitants, were being diverted at a point [76] on said stream about one-half mile south of the north line of Town-

ship 13 North of Range 19 West, Montana Meridian, the same being the point of location of defendant's diversion dam, and that said water has since prior to the date of said decree been continuously diverted at said point and used for said purpose.

IV.

That each and all of the plaintiffs in this action, with the exception of Missoula County, in so far as they own either the land or the water rights claimed by them, acquired the same and all of them long subsequent to the date of the decree in said cause No. 1953, and long subsequent to the construction of the dam and other works used for the diversion and distribution of water to the city of Missoula and its inhabitants, said dam being located as alleged in Paragraph III hereof. That Missoula County and the predecessors in interest of all of the other plaintiffs in this action, were parties defendant in said Cause No. 1953.

V.

That for the purpose of diverting the water necessary to supply the needs of defendant's predecessor in interest in furnishing water to the city of Missoula and its inhabitants, the dam and intake reservoir constructed for that purpose prior to the date of said decree, as herein alleged, was constructed at a cost of more than \$20,000.00, a distribution reservoir was likewise constructed at a cost in excess of \$20,000.00, and a pipe line was laid to carry said water from said point of diversion

at a cost in excess of \$85,000.00, and necessary rights of way were acquired at a cost in excess of \$4,000.00, and all of said works were constructed for the purpose of [77] diverting at one point the water required for distribution in the city of Missoula, and including said rights No. 1, No. 2, and No. 9, to the extent that the same were necessary, and that such diversion at one point has continued ever since that time, and still continues. That since that time many hundreds of thousands of dollars have been expended by the defendant and defendant's predecessors in interest in the improvement, extension and repair of the said works, and of the distribution system used to distribute the said water in the city of Missoula, all of which expenditures have been made in reliance upon the right of the defendant and its predecessors to make and continue said diversion at said point, and upon the acquiescence of plaintiffs and their predecessors therein.

VI.

That said works, and particularly said dam and reservoir, were and are permanent structures, the dam being placed in the stream in a prominent and conspicuous location, and that its location and its purpose were at all times known to plaintiffs and plaintiffs' predecessors in interest.

VII.

That since the year 1902 when said dam was constructed, there have been at least two distinct

changes in ownership of the said water system and water rights supplying the same, such property having been conveyed by the old Missoula Water Company to Missoula Light & Water Company, and thereafter by said company and its successor Missoula Public Service Company, to this defendant, and that each of said distinct owners acquired title in reliance upon the right to use the system and diversion works as installed in 1902, and to continue the diversion of water at the point where said dam was located, and the acquiescence in and failure to object to such use by plaintiffs and their predecessors. [78]

VIII.

That substantially all of the persons who were living and in a position to know the facts, physical and otherwise, as they existed at the time when said water rights were first diverted at the one point where said dam was located, have either died or are gone from the jurisdiction, and this defendant is informed and believes and therefore states, that most if not all of such facts are now unavailable for that reason. That the evidence taken in said Cause No. 1953 cannot be found in the records of said cause, and that the defendant after searching diligently for the same is unable to find it.

IX.

That the said source of supply is the only available source from which the people of the city of Missoula may be furnished with water, and that diversion at the old points of diversion of the Mill

ditch or the Higgins ditch referred to in the plaintiffs' complaint of water for use in the distribution system supplying the city of Missoula, is not practicable or feasible.

X.

That notwithstanding the facts set forth in this separate defense the plaintiffs and their predecessors in interest, knowing the location of the point of diversion, and knowing the use to which the water has been put, and knowing the expenditures and improvements in general that have been made in distributing said water, have acquiesced in such diversion and distribution, and have allowed and permitted large sums to be expended upon said system, and have allowed and permitted the water necessary to furnish said city and its inhabitants to be diverted at the point where it was diverted at the time the decree [79] was entered in said Cause No. 1953. That this has gone on for more than thirty years, and that no action has been brought or effort made to prevent or change the use or place of diversion or to in any way alter the method of use of water from Rattlesnake employed by the defendant and its predecessors in interest, and while this defendant alleges that it and its predecessors have at all times been entitled to divert said water at the point where it has been diverted and to use the same as it has been used, it further alleges that in any event the plaintiffs and their predecessors in interest have been guilty of laches, and in equity and good conscience are precluded and estopped from obtaining any relief sought in this action.

FOR A FURTHER ANSWER AND FOURTH SEPARATE DEFENSE, THIS DEFENDANT ALLEGES:

I.

That while it denies that the plaintiffs, or any of them, have or at any time had any cause of action against the defendant, or any of its predecessors in interest, it further alleges that if the plaintiffs or their predecessors ever had any cause of action, the same arose more than five years prior to the bringing of this action, and is barred by the provisions of Section 9041 Revised Codes of Montana for 1921.

Wherefore, having fully answered, the defendant prays that the plaintiffs take nothing in this action and that the defendant recover its costs herein expended.

W. L. MURPHY

A. N. WHITLOCK

J. E. CORETTE, JR.

Attorneys for Defendant,
Missoula Montana. [80]

State of Montana,
County of Missoula.—ss.

A. N. Whitlock being first duly sworn on oath deposes and says; that he is one of the attorneys for the defendant in the above entitled action and makes this verification for and on behalf of said defendant for the reason that it is a corporation and has no officer within the county where affiant resides; that affiant has read the foregoing answer, knows the contents thereof, and that the matters

and things therein stated are true to the best of his knowledge, information and belief.

A. N. WHITLOCK

Subscribed and sworn to before me this 18th day of October, 1933.

[Seal]

LILIAN C. WENZEL

Notary Public for the State of Montana
Residing at Missoula, Montana.

My commission expires Feb. 10th, 1936.

Service of the foregoing answer accepted and receipt of copy acknowledged this 18th day of October, 1933.

E. C. MULRONEY and
S. P. WILSON,

Attorneys for Plaintiffs.

[Endorsed]: Filed Oct. 18, 1933. [81]

Thereafter, said cause was duly tried on October 25th and October 26th, 1933, the record thereof being in the words and figures following, to wit:
No. 1488, Jackson C. Sain et al. vs. Montana Power Company.

This cause came on regularly for trial this day, Mr. E. C. Mulroney and Mr. S. P. Wilson appearing for the plaintiffs, and Messrs. W. L. Murphy, A. N. Whitlock and John E. Corette Jr. appearing for defendant.

Thereupon, on motion of Mr. Whitlock, court ordered that the name of Mr. Walter L. Pope be entered as associate counsel for defendant.

Thereupon, on motion of Mr. Wilson, there being no objection, court ordered that the complaint herein be amended by interlineations as follows: On page 2, line 8, paragraph 4, change the figures "1930" to "1903".

Thereupon, on motion of Mr. Whitlock, there being no objection, court ordered that the answer herein be amended by interlineation in accordance with written amendments filed.

Thereupon Will Cave, W. H. Sweringen, Edward Ray, J. C. Sain, Russell Miller, I. Q. Roberts, Jack Ray, Joe McDonald, C. W. Leaphart, Geo. Cromwell, L. E. Tucker, Ed Newton, W. M. Hay, Henry Bergstrom, John J. Flynn, Henry Partoll, John A. Morelles and Charles E. Quast were sworn and examined as witnesses for plaintiffs and plaintiffs' exhibits 1, 2, 3, 4 and 5 introduced in evidence. Thereupon counsel orally stipulated and agreed relative to the testimony which would have been given by certain of the plaintiffs had they been called to testify, whereupon plaintiffs rested.

Thereupon H. S. Thane, J. M. Brechbill, T. T. McLeod, C. H. McLeod, C. H. Christianson, Peter Federson, J. M. Price, G. J. Hagens and W. L. Murphy were sworn and examined as witnesses for defendant, W. M. Hay was recalled as a witness by defendant and defendant's exhibits 6 to 13, inclusive, introduced in evidence. A certain written offer of proof was made by defendant, to which the plaintiffs objected, and thereupon court ordered that said objection be sustained, to which ruling of the

court the defendant then and there excepted and exception noted.

Thereupon further trial of cause was ordered continued until 9.30 A. M. tomorrow.

Entered in open court October 25, 1933.

C. R. GARLOW, Clerk.

No. 1488, Jackson C. Sain, et al. vs. Montana Power Company.

Counsel for respective parties present as before and trial of cause resumed.

Thereupon J. C. Sain and H. S. Thane were recalled as witnesses by defendant, Arthur Sticht was sworn and examined as a witness for defendant and defendant's exhibits 14 and 15 introduced in evidence, whereupon defendant rested.

Thereupon W. H. Sweringen, Russell Miller, J. C. Sain, I. Q. Roberts, Edward Ray, L. E. Tucker, Joe McDonald, and C. W. Leaphart were recalled as witnesses in rebuttal, Roscoe Jackman and E. C. Mulroney were sworn and examined as witnesses in rebuttal and plaintiffs' exhibit 16 introduced in evidence, whereupon plaintiffs rested and the evidence closed.

Thereupon defendant moved the court to dismiss the bill of [82] complaint herein for lack of proof and that plaintiffs are barred by virtue of laches in the premises, which motion was by the court taken under advisement.

Thereupon the cause was submitted to the court and taken under advisement, plaintiffs being granted 10 days in which to file their brief, and defendant to have 10 days thereafter in which to file its brief, and both sides being granted leave to submit proposed findings of fact and conclusions of law.

Entered in open court October 26, 1933.

C. R. GARLOW, Clerk. [83]

Thereafter, on February 5th, 1934, the

DECISION

of the court was duly filed herein, in the words and figures following, to wit: [84]

[Title of Court and Cause.]

This is final hearing in a suit involving the primitive, ancient and eternal struggle for the life-giving fluid, the water-holes and springs in the desert, the streams which make fruitful and to blossom as the rose the waste places of earth.

The parties are some of the appropriators of the water of Rattlesnake Creek, one of the more delightful of Montana's many beautiful streams, despite its repellant but "Western" name. As usual, appropriations exceed the flow, and as usual, just apportionment involves difficulties inciting litigation in lieu of sometime armed foray with spear or gun.

Ignoring non-essentials of strategy, camouflage and nuisance-value, the gist of the case is whether defendant's change in place of diversion of water inflicts substantial injury on any plaintiff.

The evidence discloses appropriations by defendant in amount 1184 inches prior to any plaintiff's, 160 inches more, prior to any plaintiff's save one of 45 inches, 775 inches more, prior to any plaintiff's save the aforesaid and one of 145 inches, and some subsequent unnecessary to detail.

The change involved, made in 1902, is from the Mill ditch and the Higgins ditch, both below plaintiffs, to a dam $1\frac{3}{4}$ miles above the Higgins, $3\frac{1}{2}$ miles above the Mill and 100 feet higher, and above most of plaintiffs.

The defendant is a public utility and now diverts no water save at said dam and to serve the city of Missoula. It appears defendant has not diverted more than 1112 inches or 6 inches more than its appropriations by the ditches aforesaid and prior to all plaintiffs.

Above the dam defendant has 8 reservoirs, but claims nothing here by reason of any excess water stored. The dam obstructs all flow of the stream save overflow more or less intermittent and which varies as varies the flow and diversion by defendant. Likewise varies the [85] flow below the dam.

Taking the testimony for it and particularly that of defendant's superintendent, when defendant sometime diverts all flow, the surface flow runs off and the bed of the stream dries to a short distance

above the Higgins ditch. There and below, however, the usual sub-surface flow emerges, and always affords a surface flow of water at the head of at least the Mill ditch, in amount sometime 340 inches.

In effect, the sub-surface operates as a by-pass around plaintiffs' places of diversion, and as a tributary or accretion to the stream above defendant's before the change. This water not available to any plaintiff but available to defendant at the Mill ditch if not at the Higgins ditch, is by it permitted to waste and its equivalent taken at the dam.

And this consequence of the change is the grievance and injury of which plaintiffs complain. That complaint is justified, grievance and injury real and substantial is clear, plain as a pike-staff.

A single illustration suffices.

Assume a flow of 1000 inches at the dam, defendant's need and diversion 700 inches, and overflow 300 inches. The last enters the sub-surface and only emerges where unavailable to any plaintiff but available to defendant. Obviously, had defendant not changed diversion from the ditches to the dam, the 1000 inches in surface and sub-surface flow adown the stream would supply 300 inches to plaintiffs and 700 inches, its need and so the limit of its right, to defendant at the ditches. Therefore, at that time or any other of shortage, in just apportionment this wasted water is to be charged against defendant, its diversion at the dam limited to its need (in general, always the limit of a water right when others need water, however greater the appropriation), less any

substantial flow at the head of the Higgins and/or the Mill ditch, the deduction not to exceed the extent of defendant's resort to the priorities by said ditches obtained.

In so far as diversion at the dam lessens evaporation and absorption, defendant is to be given the benefit when needed. But that is not all.

If further appears that in a suit involving these parties and all other appropriators of the water of said stream, in 1903 in the local state court was rendered a decree settling priorities in time and [86] amount, and each party was enjoined from trespass upon any other. And to this day that court maintains and exercises jurisdiction to enforce and execute its decree by its officer (water commissioner) to apportion the water and supervise its use.

If is any good reason why the parties should invoke the interposition of this court to vindicate rights by the state court adjudicated, it has not been suggested and passeth understanding.

Why a decree, injunction, and execution here, to enforce a decree, injunction and execution there? And if secured, to enforce them why not a new suit in the state court?—and so on ad infinitum, decree upon decree imposed, like Ossa on Pelion piled.

Is not that court able to visit the just penalty on this defendant or any other who in trespass violates the court's decree and injunction, and will it not do so?

To ask is to answer.

And if that court's officer does not justly appor-tion the water (for is no evidence defendant di-verted more than he sanctioned) no doubt the court will apply the proper remedy.

It is true suit may be maintained to execute a decree in another suit in the same or another court. But only when is some valid reason, only when sub-sequent events interpose obstacles to otherwise exe-cution by the court of the first decree. That is not this case.

Equity has discretion in the matter of relief, and may grant or deny it unless circumstances convert discretion into duty. Where duty begins, discretion ends. The state court and this are of concurrent jurisdiction, each from the other entitled to the respect and deference proper between equals. That court is competent as this to finish what these parties in it began.

To solicit this court to in effect supersede the state court is an affront to both, whether or not also con-tempt. Is this court's officer to undo what the state court's officer does, and vice versa?

The practise is bad, breeds conflict, and is in-tolerable.

So far has it been carried, that in the opinion in *Simmons vs. Ry. Co.*, the last of three suits involv-ing the same stream, this court observes the three decrees result in an impasse, nullity. That is, in the first suit A is decreed prior to B, in the second suit B is decreed prior to C, and in the third suit C is

decreed prior to A,—a triple estoppel, the parties in complete circle back to the starting [87] point.

Moreover, it is settled law that suits to determine priorities in use of water partake of the quality of real actions, and so far involve a res that the court first obtaining jurisdiction of them should proceed to the determination without interference by any other court, on principles well settled between the courts of the United States and of the states.

Rickey Etc. Co. vs. Miller and Lux, 218 U. S. 262;
U. S. vs. American Etc. Assoc., 2 Fed. Sup. 867.

It is not mere matter of comity but of right. That is this case. And although neither party objected, it is the duty of the court sua sponte to avoid abuse of its authority, to refrain from invasion of the state court's jurisdiction.

Suit dismissed without costs.

BOURQUIN, J.

[Endorsed]: Filed Feb. 5, 1934. [88]

Thereafter, on April 25, 1934,

DECREE

was duly entered herein in the words and figures following, to-wit:

In the District Court of the United States in and for
the District of Montana.

No. 1488.

JACKSON C. SAIN, et al.,

Plaintiffs,

vs.

THE MONTANA POWER COMPANY,
a corporation,

Defendant.

This cause came on to be heard at this term and was submitted by counsel for decision, and thereupon, upon consideration thereof the court filed written decision therein, and in accordance therewith IT IS ORDERED, ADJUDGED and DECREED that said suit be dismissed without costs.

Dated April 25, 1934.

BOURQUIN, Judge.

[Endorsed]: Filed April 25, 1934. [89]

Thereafter, on May 3, 1934, Petition for Appeal was duly filed herein in the words and figures following, to-wit: [90]

[Title of Court and Cause.]

PETITION FOR ALLOWANCE OF APPEAL.

[91]

The above named plaintiffs feeling themselves aggrieved by the decision, judgment and decree entered in this cause on the 5th day of February, 1934, do hereby appeal to the Circuit Court of Appeals for the Ninth Circuit for the reasons assigned in the Assignment of Errors filed herewith and said plaintiffs pray that their appeal be allowed, and that citation issue as provided by law, and that the Transcript of Record, proceedings and papers upon which said decree was based duly authenticated, be sent to the United Circuit Court of Appeals for the Ninth Circuit sitting in the City and County of San Francisco, State of California, under the rules of such Court in such cases made and provided.

And *you* petitioners further pray that a proper order touching the security to be required of them to perfect their appeal be made.

Dated this 5th day of April, 1934.

E. C. MULRONEY &

S. P. WILSON,

Attorneys for Plaintiffs.

Service of the foregoing petition for allowance of appeal is hereby admitted and a copy of the same

received at Missoula, Montana, this 3rd day of May, 1934.

W. L. MURPHY,
A. N. WHITLOCK,
Attorneys for Defendant. [92]

State of Montana,
County of Missoula.—ss.

Jackson C. Sain, being duly sworn upon oath says:

That he is one of the petitioners foregoing named and he makes this verification for and on behalf of all the petitioners; that he has heard read the foregoing petition and knows the contents thereof and that the matters and things therein stated are true to the best of his knowledge, information and belief.

JACKSON C. SAIN

Subscribed and sworn to before me this 2nd day of May, 1934.

[Seal]

EDWARD C. MULRONEY

Notary Public for the State of Montana,
residing at Missoula, Montana.

My Commission expires: June 15, 1935.

[Endorsed]: Filed May 3, 1934. [93]

Thereafter on May 3, 1934, Order Allówing Appeal was duly entered herein in the words and figures following, to wit: [94]

[Title of Court and Cause.]

ORDER ALLOWING APPEAL. [95]

Upon reading and considering the petition for appeal on file herein together with the Assignment of Errors on file herein :

IT IS HEREBY ORDERED that the appeal of Jacksen C. Sain and the other plaintiffs to the United States Circuit of Appeals for the Ninth Circuit be, and the same is hereby allowed, upon the filing of a good and sufficient bond in the sum of \$300.00 to be approved by the Court.

Dated this 3rd day of May, 1934.

BOURQUIN,
Judge.

Service of the foregoing order allowing appeal is hereby admitted and a copy of the same received at Missoula, Montana, this 3rd day of May, 1934.

W. L. MURPHY

A. N. WHITLOCK

Attorneys for Defendant.

[Endorsed]: Filed May 3, 1934. [96]

Thereafter, on May 3, 1934, Prayer for Reversal was duly filed herein in the words and figures following, to wit: [97]

[Title of Court and Cause.]

PRAYER FOR REVERSAL. [98]

Come now the plaintiffs in the above-entitled action and pray that the decision, judgment and decree entered herein in the District Court of the United States in and for the District of Montana on the 5th day of February, 1934, be reversed by the United States Circuit Court of Appeals for the Ninth Circuit and that such other and further orders as may be fit and proper in the premises be made in the above-entitled cause by said Circuit Court of Appeals.

Dated this 5th day of April, 1934.

E. C. MULRONEY &
S. P. WILSON

Attorneys for Plaintiffs.

Service of the foregoing prayer for reversal is hereby admitted and a copy of the same received at Missoula, Montana, this 3rd day of May, 1934.

W. L. MURPHY
A. N. WHITLOCK

Attorneys for Defendant.

[Endorsed]: Filed May 3, 1934. [99]

Thereafter, on May 3, 1934, Assignment of Errors was duly filed herein in the words and figures, following, to wit: [100]

[Title of Court and Cause.]

ASSIGNMENT OF ERRORS. [101]

Come now the plaintiffs in the above-entitled cause and file the following Assignment of Errors upon which they rely in the prosecution of their appeal from the decision, judgment and decree in said suit made and entered by the above-entitled Court on the 5th day of February, 1934.

I.

The Court erred in dismissing plaintiffs' Bill of Complaint.

II.

The Court erred in finding and holding that the Court is without jurisdiction in the cause.

III.

The Court erred in finding and holding that the State Court and not the United States Court has jurisdiction to hear and determine the matters at issue as shown by the pleadings in the cause.

IV.

The Court erred in finding and holding that to entertain this suit and decide the same in accordance with justice and the rights of the parties would constitute an invasion of the jurisdiction of the State Court.

V.

The Court erred in finding and holding that plaintiffs may not have an injunction and restraining order in this cause as prayed for in the complaint in this cause.

VI.

The Court erred in finding and deciding against the plaintiffs in this action and in favor of the defendant.

VII.

The Court erred in granting to the plaintiffs the injunction and relief prayed for in the complaint.

VIII.

The Court erred in not finding each of the proposed [102] findings of fact that were requested by the plaintiffs, to be true, the same being numbered Findings of Fact requested by plaintiffs numbered 1 to 19, inclusive, and the Court erred in failing to find and decide that each and all of said proposed Findings of Facts are true.

IX.

The Court erred in not finding and deciding that defendant herein has the legal right to divert from Rattlesnake Creek at the place designated on the maps introduced in evidence in this cause as "Dam" to the extent that it has need therefor, the water awarded and adjudicated to its predecessors in the decree in Cause No. 1953 by rights Nos. 3, 8 and 14 of the Findings of Fact in said decree and within the limits and according to the priorities prescribed in said decree, for the purpose of supplying the city of Missoula and its inhabitants with

water, but defendant does not have the right to divert at said place designated or said maps as "Dam" water to satisfy any of the other decreed rights included or adjudicated by the decree in Cause No. 1953 to its predecessors, whenever plaintiffs have need for such water.

X.

The Court erred in not finding and deciding that the attempt by defendant and its predecessors in interest to change the place of diversion of Right No. 1 in the Findings of Fact in the decree in Cause No. 1953 from the head of the Mill ditch to the "Dam", and likewise the attempt of defendant and its predecessors in interest, to change the place of diversion of Right No. 2, in the Findings of Fact of the decree in Cause No. 1953, from the head of original Higgins ditch to the "Dam"; and likewise the attempt of defendant and its predecessors in interest to change the place of appropriation of Right No. 9 in the Findings of Fact of the decree in Cause No. 1953 from the [103] head of original Higgins ditch to the "Dam" are, and each of said attempts is, injurious to plaintiffs, and said attempts cause, and each said attempts causes, damage and prejudice to plaintiffs and all of plaintiffs.

XI.

The Court erred in not finding and deciding that plaintiffs are entitled to an injunction restraining defendant from making the changes in place of diversion of the water rights described in the complaint in this action and referred to in these findings, or making either or any of such changes, when-

ever plaintiffs or any of plaintiffs shall be unable to obtain water at his or their point of diversion on account of defendant's diversion, said plaintiff or plaintiffs then having need for such water. Particularly plaintiffs shall be entitled to enjoin and restrain defendant from changing the point of diversion of right No. 1 of the Findings of Fact in the decree in Cause No. 1953 from the head of the Mill ditch to the "Dam", and shall be entitled to enjoin and restrain defendant from changing the point of diversion of right No. 2 of the Findings of Fact of the decree in Cause No. 1953 from the head of the original Higgins ditch to the "Dam", and shall be entitled to enjoin and restrain defendant from changing the point of diversion of Right No. 9 of the Findings of Fact of the decree in Cause No. 1953 from the head of original Higgins ditch to the "Dam", at any time whenever plaintiffs or any of plaintiffs have need for the water to satisfy their own appropriations and are unable to obtain the water to satisfy their own appropriations because of defendant's diversion thereof.

XII.

The court erred in not finding and deciding the claim of defendant to have the right to change the point of diversion of the water awarded and decreed to its predecessors in interest [104] in Findings 1, 2 and 9, from the head of the Mill ditch and original Higgins ditch to the "Dam", is wrongful and without authority of law and is invalid, being injurious to plaintiffs, and defendant shall not have the right to make change of the point of diver-

sion of said water rights, nor any thereof, whenever plaintiffs, or any of plaintiffs, have need for such water and are deprived of the water on account of any diversion of water by defendant.

XIII.

The Court erred in not finding and deciding that the plaintiffs were not guilty of laches, either in the commencement of their suit, or in the prosecution thereof, and that the plaintiffs' right of action set forth in the pleadings herein against the defendant is not barred by laches.

XIV.

The Court erred in not finding and deciding that the plaintiffs' action was instituted in good time and is not barred by the statute of limitations.

XV.

The Court erred in not finding and deciding the issues herein in favor of plaintiffs and against defendant.

WHEREFORE, plaintiffs pray that the decree herein be reversed.

E. C. MULRONEY &
S. P. WILSON,

Attorneys for Plaintiffs.

Service of the within Assignment of Errors is hereby admitted and a copy thereof received at Missoula, Montana, this 3rd day of May, 1934.

W. L. MURPHY,
A. N. WHITLOCK,

Attorneys for Defendant.

Thereafter, on May 3, 1913, Bond on Appeal was duly filed herein in the words and figures following, to wit: [106]

[Title of Court and Cause.]

BOND ON APPEAL. [108]

KNOW ALL MEN BY THESE PRESENTS:

That we, Jacksen C. Sain, in his own behalf and on behalf of all the plaintiffs above named, as principal, and St. Paul Mercury Indemnity Company, a corporation, organized and existing under and by virtue of the laws of Minnesota and qualified and authorized to do business in Montana, to execute bonds and undertakings and to act as security generally, within the District and State of Montana, are held and firmly bound unto Montana Power Company, a corporation, the defendant above named in the full sum of Three Hundred Dollars, to be paid to the said defendant, its successors or assigns to which payment well and truly to be made, said principal and said surety bind themselves, their, and each of their, successors and assigns, jointly and severally, firmly by these presents.

Sealed and dated this 3rd day of May, 1934.

WHEREAS, in the District Court of the United States for the District of Montana in the above-entitled suit pending in said Court between the above named plaintiffs and the above named defendant, a decision, judgment and decree was rendered against the said plaintiffs upon the 5th day of February, 1934, which judgment was entered on the 5th day of February, 1934, and said plaintiffs have petitioned for an appeal from said decision,

judgment and decree to the Circuit Court of Appeals of the United States for the Ninth Circuit and said plaintiffs propose to prosecute said appeal to reverse the said decision, judgment and decree and answer all costs if they fail to make their plea good.

NOW, THEREFORE, in consideration of said appeal, the condition of this obligation is such that if the plaintiffs shall prosecute their said appeal to effect and answer all costs if they fail to make good their plea, then this obligation shall [109] be void, otherwise to remain in full force and effect.

JACKSON C. SAIN

[Seal] ST. PAUL MERCURY INDEMNITY
COMPANY

By S. P. Wilson, Agent.

The foregoing bond approved this 3rd day of May, 1934.

BOURQUIN,
Judge.

[Endorsed]: Filed May 3, 1934. [110]

Thereafter, on May 3rd, 1934, Citation was duly issued herein, which original citation is hereto annexed and is in the words and figures following, to wit: [111]

[Title of Court and Cause.]

CITATION. [112]

United States of America to Montana Power Company, a Corporation, Greeting:

You are hereby cited and admonished to be and appear in the United States Circuit Court of Ap-

peals for the Ninth Circuit to be held at the City of San Francisco, California, within thirty days of the date hereof pursuant to an order filed and entered in the office of the Clerk of the District Court of the United States for the District of Montana, allowing an appeal from a decision, judgment and decree filed and entered in said Court on the 5th day of February, 1934, in favor of the defendant and against the plaintiffs in the above-entitled action being In Equity Number 1488, wherein you are the defendant and the above named plaintiffs are the plaintiffs, to show cause, if any there be, why the decision, judgment and decree rendered against the said plaintiffs, as in said appeal mentioned, should not be reversed and corrected and why justice should not be done the parties in that behalf.

WITNESS the Honorable George M. Bourquin, Judge of the United States District Court for the District of Montana, the 3rd day of May, 1934.

BOURQUIN,
Judge.

Service of the foregoing citation admitted and a copy thereof received at Missoula, Montana this 3rd day of May, 1934.

W. L. MURPHY,
A. N. WHITLOCK,
Attorney for Defendant.

[Endorsed]: Filed May 3, 1934. [113]

Thereafter, on May 3rd, 1934, Statement of the Evidence was duly approved and filed herein, which is Vol. 2 of this transcript and consists of pages 116 to 296 inclusive. [115]

[Title of Court and Cause.]

PLAINTIFFS' PROPOSED STATEMENT
OF EVIDENCE. [116]

BE IT REMEMBERED: That the above entitled action came regularly on for trial in said court at Missoula, Montana on Wednesday, the 25th day of October, 1933, before the Honorable George M. Bourquin, sitting without a jury upon the pleadings theretofore filed in said action. The Plaintiffs were represented by E. C. Mulroney, Esq., of Missoula and S. P. Wilson, Esq., of Deer Lodge; the defendant was represented by Messrs. Murphy & Whitlock and John E. Corette, Jr., Esq. and Walter L. Pope, Esq., all of Missoula. Thereupon the following proceedings were had and taken and the following evidence and none other was introduced:

PLAINTIFFS' CASE IN CHIEF.

PLAINTIFFS' TESTIMONY.

WILL CAVE

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is Will Cave. My residence is at Missoula, Montana, where I have lived for 60 years. I know Higgins Ditch out of Rattlesnake Creek and Mill Ditch. I first became acquainted with the

(Testimony of Will Cave.)

lower portion of the Higgins Ditch in 1873, and the upper portion where it takes water out of Rattlesnake Creek some two or three years later, I cannot remember the exact time, but I do remember, as a boy, fishing along the creek by the head of this ditch. A few days ago in preparation for the trial of this case I pointed out to William Swearingen, plaintiffs' engineer, the head of the original Higgins Ditch and also the head of the Mill Ditch. [117]

CROSS EXAMINATION by Mr. Pope:

I am familiar with the location of the Fedderson (now Klapwyck) barn, the head of the old Higgins Ditch is about a quarter of a mile down stream from this barn and about 200 yards north of the south line of section 10, which I think was the Fedderson land. The head of the Mill Ditch was right under the Northern Pacific trestle crossing the Rattlesnake. A little over a quarter of a mile above the head of the Higgins Ditch, Rattlesnake creek divides into two channels, the forking of the stream to make two channels, being a little north, up stream, of the Fedderson or Klapwyck barn.

W. H. SWEARINGEN,

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is W. H. Swearingen, and my residence, Missoula, Montana. My occupation, Civil

(Testimony of W. H. Swearingen.)

Engineer, which occupation I have been engaged in practically all my life. I am now city engineer of Missoula. I made a map in the past few days showing various ditches out of Rattlesnake Creek; Rattlesnake is located northerly from the City of Missoula, and in Missoula County. It is a tributary of the Hellgate or Missoula River or Clark's Fork, emptying into the Missoula River within the Dan Paul Addition to Missoula about 300 feet west of the Van Buren Street bridge. The map shows the Rattlesnake Creek to its mouth, also the Mill and original Higgins ditches; the points of diversion of these ditches were pointed out to me by Will Cave to enable me to prepare the map. The map also shows the Hamilton-Grant-Day [118] ditch, which is on the west side, as are the Higgins and Mill ditches, and on the east side there is the Tucker, Williams, Cobban, Fedderson and Neill ditches, all of which are named on the map. The map also shows the lands of the various plaintiffs, which lands are generally indicated by the name of the owner, and a color so far as possible for each separate holding. My information for the separate holdings of each of the plaintiffs was taken from the complaint. The holdings of the smaller owners among plaintiffs are not entirely accurately shown on the map, because such holdings in some instances are so small that the same cannot well be shown on so small a scale.

(Testimony of W. H. Swearingen.)

The head of the Mill ditch is approximately 1000 or 1500 feet north (above) the mouth of the creek; the original Higgins ditch is located directly opposite the valve house on the Montana Power Company pipeline, and it is in section 11, north of the south line of 11 about an eighth of a mile. The "dam" is approximately four miles (up stream) from the head of the Mill ditch. The "dam" that I speak of has to do with the defendant's diversion of water; the "dam" collects all the water in the creek and defendants can let as much go over the dam and down the creek as it wants to, but defendant is able to divert the entire flow from the creek into its pipeline, which runs into its reservoir, from which water is taken for distribution to the City of Missoula. The Fredline ditch heads out of Rattlesnake creek about a mile above the head of Mill ditch and below the head of Higgins ditch.

The map substantially correctly shows these things, and the approximate location of those ditches.

Whereupon, without objection, the map is offered and [119] admitted in evidence as plaintiffs' Exhibit 1.

CROSS EXAMINATION by Mr. Whitlock:

The location of the Higgins and Mill ditches was obtained from someone else, not from my own knowledge, and the location of the other ditches, designated by name, was made by me from actual observation on the ground, merely approximately.

(Testimony of W. H. Swearingen.)

By defendant's point of diversion, I mean the "dam". It extends entirely across the creek, so that the whole creek can be diverted, though it has gates permitting the water to flow through it. The "dam" is approximately 100 feet higher in elevation than the head of the Mill ditch. The head of the Mill ditch is approximately on a level with the lower part of the City of Missoula, and the head of the Higgins ditch is at a lower level than the "dam".

REDIRECT EXAMINATION by Mr. Wilson:

My location, with the help of Mr. Cave, of the heads of the Higgins ditch and Mill ditch, as well as the ditches on the east side of the creek was made by me by personal observation on the ground.

EDWARD RAY,

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is Edward Ray; I live up Rattlesnake about 5 miles and am a dairy man. I have lived there 12 years, and my home is on the old Effinger place. I have water rights, 100 inches of Spring Gulch of 1882 and 100 inches of Rattlesnake of 1889, which latter right is No. 17 in Rattlesnake decree. I have not yet received a deed for my land, because I have not yet fully paid the purchase price, but I

(Testimony of Edward Ray.)

hold a contract of [120] purchase for it, legal title still standing in the name of Charlie Effinger. I have participated in the making of observations and measurements in the last few years along Rattlesnake creek. In 1926 we had a weir in the creek, where the Mill ditch takes out.

Q. How wide was the weir that the water flowed over?

A. Well, I believe it was six feet.

Q. Now, how much water, do you recall, was flowing over the weir?

Mr. WHITLOCK: That is objected to, if your Honor please, as not material to this case, relating to a measurement long subsequent to the alleged time of the change of diversion; and besides, it is objected to for the reason that this man is not the man who made the measurement.

The COURT: Overruled.

Mr. WHITLOCK: Note an exception.

On August 12th, in company with Elmer Hughes, who is an engineer, we made a measurement at the head of the Mill ditch and there was then a depth of four and a quarter inches of water flowing over the weir. Elmer Hughes became afflicted with heart disease and had to go southwest, so he is not here. After we made this measurement we went immediately up stream to see the condition of the stream above, and at the lane between Rutledge Parker and Klapwyck's, which is about 100 feet below the head of the Hollenbeck ditch, there was no water in the creek. We made another observa-

(Testimony of Edward Ray.)

tion later in August and there was less water flowing over the weir at the head of the Mill ditch than there was on August 12th, but the stream was dry 100 feet below the head of the Hollenbeck ditch, where we made an obser- [121] vation. The water at the weir came up probably from the dam.

During the time these observations were being made, the ditch on the east side of the creek, coming out by Van Buren Street, which I think is named Fredline ditch, was always running full, and the size of the stream can be determined, because it went through some round pipes, which I did not measure.

Q. Now, Mr. Ray, since you have been up there have you—just tell us the condition of the stream bed below the dam during the summer months, say in the month of August, as to water raising, if you have ever observed, in the channel. Just describe what—how it comes.

Mr. WHITLOCK: That is objected to as relating to a time not material to the time of the alleged change in diversion, this witness saying he has recollection or knowledge no further back than 12 years.

The COURT: Overruled.

Mr. WHITLOCK: Exception.

Water arises in the bed of the stream below the head of the Hollenbeck ditch. It starts to raise up in the bed of the stream where the county bridge crosses, which is about two or three hundred feet below the head of the Hollenbeck ditch. The water

(Testimony of Edward Ray.)

comes up in the creek bottom, because there are no tributaries, ditches or pipes coming in from the sides that I have seen, and I have observed it there a good many times. My residence and irrigated land is located on Rattlesnake creek above the dam of Montana Power Company. 1921 was the first year I irrigated, and I have irrigated every year since 1921. In 1921, 1922 and 1923, I always had the water decreed for my land and used that amount of water all summer each of those years. In latter August, 1924, defendant's pre- [122] decessor shut off my water for a part of the irrigation season, and we had controversies about the use of the water. The same thing was done in 1925 somewhat earlier in the season, and this was repeated in 1926 as early as July. There was trouble between me and the water company representative as to the use of the water, and other irrigators had trouble with the water company's representative. From August 1924 until the commencement of this action the water company has been increasing its use of the water and shutting down my water earlier each year. I was only shut off about 10 days in 1933. My land requires irrigation.

CROSS EXAMINATION by Mr. Whitlock:

I live above the dam of the Montana Power Company.

When I first began my residence on Rattlesnake creek Montana Power Company dam was there just like it is now in the same location, and defendant's

(Testimony of Edward Ray.)

predecessor was diverting the water there for Missoula City and its inhabitants, of which I had knowledge. I claim 100 inches of right No. 17. Concerning the measurements testified to by me, the first one was about July 25, 1926. After measuring at the weir at the head of the Mill ditch, I drove up the road to Day Bridge on Parker Lane, crossing the Rattlesnake, which is a mile and a half below the dam. I saw engineer Hughes measure the height of the water on the weir and it was around five inches in depth. Our next measurement was August 12, 1926 at the weir at the head of Mill ditch, and the water flowing over the weir was then four and a quarter inches, and after making that measurement we again went up the stream to the bridge on Parker Lane and the stream "bed" was there dry. Our third measurement was in the latter part of August, 1926, near the 29th. The depth of water then flowing over the weir was [123] around four inches. The water was a little lower at each of these measurements. We then again went up the stream to where Parker's Lane (Day bridge) crosses, and observed that the stream was dry at that point. The place up stream where we observed there was no water, where Parker Lane crosses (Day bridge) is about 100 feet below where Hollenbeck ditch comes out and a mile and a half downstream from the defendant's dam. Our measurements each day were made between 10 and 11 o'clock A. M. Fredline ditch, each of these days, was flowing full of water and getting the benefit of the water

(Testimony of Edward Ray.)

in the stream at its head. There are no streams coming into Rattlesnake creek anywhere below the dam to the mouth of Rattlesnake.

After I came to live on Rattlesnake, from 1926 on, each year, there was a water commissioner, and each year the condition as to my water, became a little worse.

It was agreed in open court between respective counsel that the Effinger land and water right No. 17 referred to in decree of Rattlesnake creek passed by mesne conveyances to the witness Edward Ray, and that he now holds same by virtue of his contract of purchase.

JACKSON C. SAIN,

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is J. C. Sain. I live on Rattlesnake where I have lived for 30 years. My occupation, florist. I am one of the plaintiffs and have 50 acres of land. I have 18th right on Rattlesnake creek for 50 inches and 36 inches of right No. 21. The 18th right was decreed to William Neill, [124] and his land and water right were acquired by me by purchase and I hold legal title to that by deed. I receive the 18th right water through the Neill ditch and the 21st right water through the Cobban-Ray-

(Testimony of Jackson C. Sain.)

mond ditch. I have made measurements of water on Rattlesnake creek during the past few years. About a half dozen of us water users on Rattlesnake made a measurement in July, 1926. Mr. Miller and Mr. Tucker's hired man were there; I cannot recall the others. Our measurement was made at the same weir in the stream at the head of Mill ditch, described by Mr. Ray. It was a 10 foot weir rather than a 6 foot weir. The water was closely dammed up so as to flow all over the weir.

Q. All right. Now, just tell us the flow of water that you observed on the day that you observed it?

Mr. WHITLOCK: That is objected to as not material to the case.

The COURT: Overruled.

Mr. WHITLOCK: Exception.

There was a peg flush with the top of the weir and there was four and a half or five inches depth of water flowing over the weir. After making this measurement, we went up stream to the head of the Hollenbeck ditch, which was taking water out. There was no water in the stream bed below the Hollenbeck ditch. We observed the stream below the head of Hollenbeck ditch and down to where this weir is located; the stream was dry below the head of Hollenbeck ditch and as you come down the water picks up in the bed of the creek. Sometimes there is a little trickling through between the banks, seeps in as we call it, but there are no tributaries coming into Rattlesnake at all, nor other sources of water

(Testimony of Jackson C. Sain.)

flow contributing water in substantial amounts to the stream, except [125] seepage from the bed of the stream, as we call it, between the head of Hollenbeck ditch and the weir; the only other water going out of the bed of the creek was the Fredline ditch. This was probably 150 inches, although we didn't measure it. There is a place on Fredline ditch, where it crosses Vine street, where the water is confined in a pipe or tube, and since then I have measured that tube and it is 18 inches in diameter and 14 inches long, laid with a good slant or grade. The ditch was not flowing full at the time of our measurement at the weir. We did estimate the flow in miners inches in the Fredline ditch at that time.

At the time of our measurement the water flowing through the weir at the head of Mill ditch was flowing into the Missoula River, and the water flowing into the Fredline ditch was going to the Highes gardens. At times being a little younger ditch, I was a little short sometimes, probably sometimes in the latter part of July I would be shut off for awhile but as a rule I got water right along.

During the first ten or fifteen years that I lived on Rattlesnake, we generally had water most every year until about 8 or 9 years ago, and then the water situation began to get a little worse. Montana Power was taking more water. My land is arid and requires irrigation.

CROSS EXAMINATION by Mr. Whitlock:

My land is located about a mile down stream from the defendant's dam. I was not a party to Rattle-

(Testimony of Jackson C. Sain.)

snake water suit, but defendant's dam was located in its present location when I began my occupancy of my land there, and water for Missoula city was then being diverted there, which facts I knew when I acquired my property. The head of the Neill ditch is approximately half a mile down stream from defendant's dam.

I participated in three water measurements in 1926, the exact days I do not remember, and part of these occasions [126] were the same as that Ed Ray testified about, one in July and one about the middle of August, and the measurement was at the weir at the head of Mill ditch. The depth of water flowing over the weir was from four and a half to five inches, and each measurement showed the flow slightly lower than the previous flow. We did not go to any point on the stream, except the point described below the Hollenbeck ditch, which is approximately a mile and a half down stream from the dam. The occasions mentioned were the only observations made at the stream, but we made observations at the Fredline ditch, and once there was water flowing in that. The water in the bed of the stream below the Hollenbeck ditch was seepage water. I say we had water until the last 8 or 9 years for our use in irrigation, but it was not plentiful. Some years we had all that was coming, and other years our ditches were shut down when it got dry, but for the first 10 or 15 years I lived up there, we got practically all our decreed water, but for the

(Testimony of Jackson C. Sain.)

last 8 or 9 years there have been times we were short of water. I know how much water Montana Power has taken some years. We measured in August, 1923 at the weir at the head of the dam and we made other measurements later. When I said that Montana Power has used more water in the last 8 or 9 years than it used prior to that time I was merely stating my assumption and belief.

REDIRECT EXAMINATION by Mr. Wilson:

The year I began my residence on Rattlesnake creek was about 1907. The water flowing in the Fredline ditch at the time of our measurement in August, 1926 was seepage water taken out of the bed of Rattlesnake creek. The measurement of stream flow made in August, 1933 at the head of defendant's dam was 1100 [127] inches.

RUSSELL MILLER,

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is Russell Miller. I live on Rattlesnake creek and have lived there since March 1, 1915. I have 10 acres of land. I have portions of water rights 10 and 16 of Rattlesnake decree, and a portion of right 20 between me and my sister, all through Hollenbeck ditch; my land requires irriga-

(Testimony of Russell Miller.)

tion. I participated in the making of a measurement of water flow of Rattlesnake creek and I made a memorandum of it at the time, and the measurement was upon July 15, 1926. There was a body of men on that day finishing a dam and placing a weir on the creek at the head of Mill ditch. These men seemingly had worked the previous day, but I came the second day. These men were J. C. Sain, L. E. Tucker, my father, L. F. Miller, Mr. Ray's hired man, and Mr. Tucker's hired man. The weir installed was 10 feet wide.

Q. All right then. Just tell us the condition of the flow of water at the point.

A. Well, the flow of water was——

Mr. POPE: We object to that upon the ground that it relates to a period not in issue in this case.

The COURT: Overruled.

Mr. POPE: Exception.

There was a depth of four and a half inches of water flowing over the weir, which is a 10 foot weir. After making this measurement, and later in the afternoon, I went up the Fredline ditch, which is one of the lower ditches, where it [128] crosses Van Buren street. It was running practically full; I estimated 100 inches, but did not measure; and when I got home, I went over to the Hollenbeck ditch around supper time and below Hollenbeck ditch there was nothing but pools, no flowing water, and I could see perhaps 20 rods down stream below the head of Hollenbeck ditch and there was nothing

(Testimony of Russell Miller.)

but potholes with water in them. The Hollenbeck dam is constructed to take all the water in the stream at that point into the ditch. When the stream is dry just below the head of Hollenbeck ditch, the amount of water in the stream bed gradually increases, so that there is always a flow before you get down to the head of the Fredline ditch. I have never seen the Fredline ditch dry; I passed over it daily for years and never remember seeing it dry; it is usually a full stream. The Fredline ditch heads away down below the head of the original Higgins ditch.

CROSS EXAMINATION by Mr. Pope:

I acquired my land about 1921 in a trade with my father. I had lived on Rattlesnake from 1915 until then, and I went constantly to my father's place. I paid no attention to the water used by the water company during my first acquaintance with Rattlesnake valley, because we just came from the east where rain fall is plentiful and water rights mean nothing, but prior to 1921, I had observed that the water company used its dam to divert water to supply Missoula.

The time of our measurement of water at the weir at the head of Mill ditch was 3:50 P. M., July 15, 1926. I helped finish the weir on that day, but the others had worked on it the previous day. That is the only measurement in which I participated. [129]

WINANS—Foillow Dick—number three

(Testimony of Russell Miller.)

DEDIRECT EXAMINATION by Mr. Wilson:

I have said that I passed the Fredline ditch practically every day and observed water flowing in the Fredline ditch, and I crossed Rattlesnake creek at the Greenough place which is just a little above where the weir measurements were made at the head of the Mill ditch, and I can never remember seeing the creek dry at that place. My judgment is that the water has always flowed there, and the water flowing there goes to the mouth of Rattlesnake creek into Hellgate river.

RECROSS EXAMINATION by Mr. Pope:

After making the weir measurement on July 15, 1926, I went to the head of the Hollenbeck ditch after supper, and in the evening sometime, it might have been right after I got home, or it might have been 8:00 or 9:00 o'clock, I don't remember the specific hour, I went to the head of the Hollenbeck ditch to ascertain whether the water flowing where we measured was seepage or whether it wasn't, and that depended on whether it was dry above or not. The water flowing in the Hollenbeck ditch at that time was a usual condition. I estimated it 40 inches, which was seepage water that had accumulated very close to the head of the Hollenbeck ditch.

I. Q. ROBERTS,

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is I. Q. Roberts. I live up Rattlesnake. My occupation is farmer. I have lived up Rattlesnake 31 years and have used decreed water, 15 inches out of Cobban-Raymond ditch and three inches out of Williams ditch. I occupy and [130] work five acres, which require irrigation. I have irrigated and grown crops during the 31 years I have lived up there. I participated in making a measurement on one occasion at the weir at the head of the Mill ditch. I had a record of it, but I misplaced it or lost it; but one measurement was between four and five inches, by that I mean there was four and a quarter or maybe four and a half inches depth of water flowing over the weir. I do not recall the width of the weir. I did not go up the stream to make observations of the stream flow above, only what I could see coming down over the railroad trestle, in the creek.

My land requires irrigation, and after the first year, I have got water through the Williams ditch during the 31 years I have resided there. The right was decreed, but the ditch was not established the first year. Since then I have been able to get my water through the Williams ditch, which has been shut off only for short periods, about half a day from time to time. The Williams ditch taps Rattlesnake above the defendant's dam.

(Testimony of I. Q. Roberts.)

I remember the original Higgins ditch about the time the Rattlesnake decree was entered. It used to cross Spruce street here in Missoula and flow west of town, and during my first years on my place on Rattlesnake, I peddled vegetables and fruit into town, and I saw the water flowing down the Higgins ditch through town every day. This was the second or third year I was up there, and I have been up there 31 years; it must have been about 1904, that is when I observed the water in the ditch across the road, and I recall seeing the water in the summer of 1904, but I do not recall when the water ceased to flow in the Higgins ditch. [131]

CROSS EXAMINATION by Mr. Whitlock:

I was not a party to the Rattlesnake water suit. My rights were acquired since then from others. I do not remember the year the measurement was made that I saw. I think Mr. Sain was present when it was made, and probably Mr. Tucker. I have had water through the Williams ditch practically all the time, but a shortage in the Cobban ditch sometimes. I do not remember the years, but during dry years; during the first few years I was up there, the ditch was never shut off. The shortage must have begun 10 years ago.

JACK RAY,

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is Jack Ray; I am employed by a banking institution, but do engineering as a side line. I have made observations of the stream flow from time to time in Rattlesnake creek. On August 7, 1924 I measured at the present intake of Montana Power Company pipeline.

Q. And what did you measure at that time?

Mr. POPE: That is objected to as relating to a period not in issue in this case.

The COURT: What is the object?

Mr. WILSON: Well the object is to show the condition of the stream, the size of the stream and the amount of water flowing.

The COURT: Well, how will this contribute to it?

Mr. WILSON: Well, upon this theory, that it is important, I suppose, to know how large a stream [132] this is, the extent and the flow of the stream. Now, what it was at the time he made his measurements and what it is now and what it will be—

The COURT: Well, is this pipeline intake out of the dam?

A. Yes, sir.

The COURT: Well, I can't see where that will show you anything about the stream. However, he may answer.

(Testimony of Jack Ray.)

Mr. POPE: Exception.

The total flow of the creek on August 7, 1924 was 1642.32 miners inches. Measurement was made at four different places, all above the dam; and the figure I have given is the entire flow of Rattlesnake creek at that time.

CROSS EXAMINATION by Mr. Pope:

At the time of my measurement, I took a cross section of all the water that was constituting the total flow of the stream, the same being a flume, a ditch, and ditch and a pipe from the flume. My measurements were made within a quarter of a mile above the intake of the defendant's water system. I couldn't say whether or not there was storage water or water from a lake or lakes back in the mountains then flowing down the stream. I believe there are several lakes back in the mountains used for storage purposes, but I have knowledge of them only by hearsay.

REDIRECT EXAMINATION by Mr. Wilson:

When there is a depth of four and a half inches of water flow over a 10 foot weir, there is 304 miners inches in the flow; when the water depth is five inches over a 10 foot [133] weir, there is 368 miners inches.

RECROSS EXAMINATION by Mr. Pope:

My answer is based on an 0.0 velocity, and assuming that the water is at a standstill seven feet above the weir.

JOE McDONALD,

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is Joe McDonald, and I reside on Rattlesnake. I am a dairyman by occupation. I have lived there since February 1, 1931. Of water rights I have 45 inches of decree right No. 5, 40 inches of No. 10, 220½ inches of No. 20, and 56 inches of No. 21. I irrigate approximately 175 acres, all of which require irrigation. During the years I have lived on Rattlesnake, I have irrigated whenever water was available. Legal title to the land possessed by me is in the name of the Federal Land Bank of Spokane, and I have a contract of purchase.

On August third of this year, with Mr. Miller, Mr. Sain and Ed Ray, we observed the stream flow of Rattlesnake creek from the head of Hollenbeck ditch to the mouth, below the head of Hollenbeck ditch; the stream bed was practically dry, no water, only potholes in the bed of the creek. We observed that the Fredline ditch was running practically full. We did not measure water flowing at the head of the Mill ditch, only observed the flow going down the stream at that point. The weir that had been installed in 1926 being no longer there. There was then a substantial flow going down the creek past the head of the Mill ditch to the mouth of the creek. The water that was flowing down by the head [134] of the Mill ditch, and that was flowing into the Fredline ditch

(Testimony of Joe McDonald.)

was seepage arising in the creek bed, below the head of the Hollenbeck ditch. My observation was that this seepage begins to come back into the channel of Rattlesnake creek below what has been described here as the head of the Higgins ditch, and below what has been described as the Day bridge, is where it starts to seep. The Fredline ditch takes out above the Day bridge and below the point of diversion of the Higgins ditch; there it is running full. The Fredline ditch sometimes, not always, exhausts the stream at the point where it diverts from the stream, and then below, the water again comes up in the channel between that and the head of the Mill ditch.

The first year I was on the creek we had an abundance of water until July, when we were abruptly shut off, to our considerable damage, and the water was not turned on again until September, I believe. In 1932, the water was not shut down quite so early, and some of the water was never completely off. This year there has been water most of the time; No. 21 was shut down a little while.

Q. I will ask you this question for the purpose of the record: to state whether or not you have suffered damage and will suffer damage in the future by reason of the change of point of diversion by the defendant from the diversion at the head of the Mill ditch or the original Higgins ditch to a point at the dam which is described by the witnesses?

Mr. WHITLOCK: That is objected to as calling for an opinion which the witness is not competent to give, and not proper.

(Testimony of Joe McDonald.)

The COURT: I think so. The facts will show. Sustained.

CROSS EXAMINATION by Mr. Whitlock:

When I acquired my land about February 1, 1931, de- [135] fendant's dam in Rattlesnake was right where it is now, and I knew that the water company was taking water from Rattlesnake. I have been at the dam several times; it is a permanent structure, apparently having been there a long time. The only time I have participated in observations of the stream flow near the head of the Mill ditch, was August third of this year. Below Hollenbeck ditch, there was just some potholes of water. I referred to seepage as the water coming out from the side of the bed of the stream; there is no flow of water that runs into the stream. This water that I speak of at the head of the Fredline ditch can be seen coming from the side, seeping out of the bank and running into it as seepage water. That condition is along there for a quarter of a mile. Water is found in potholes in the bed of the stream right at the Hollenbeck headgate, and some more water lower down, also in the bed of the stream.

REDIRECT EXAMINATION by Mr. Wilson:

Q. I will ask you, Mr. McDonald, if you observed this condition, that the creek bed would be dry just below the dam and at the same time that the water would raise above the head of the Hollenbeck ditch to make a stream flow into the Hollenbeck ditch?

(Testimony of Joe McDonald.)

Mr. WHITLOCK: That is objected to, first, as leading——

The COURT: Yes, yes. Sustained.

Mr. WILSON: Well, May I ask the witness——

The COURT: Well, he is pretty well primed for it now.

The Court takes it into consideration.

Q. Above the Hollenbeck ditch there have you observed that was the condition of the stream?

Mr. WHITLOCK: That is objected to, no time being fixed [136] and the inquiry going to a time not material in the case.

The COURT: He may answer.

Mr. WHITLOCK: Exception.

The condition of seepage water below the dam is the same as below the head of Hollenbeck ditch; below the dam there is a pipe line that dumps some seepage water in and makes a little stream, and on down below the point where the Raymond-Cobban ditch is there will be a larger stream at a time when there is no water right directly below the dam, and the Cobban ditch is a quarter or maybe a half mile down the stream from the dam, and then gets more water below the Cobban ditch until it gets to the Hollenbeck ditch.

Rattlesnake valley is approximately a mile up stream from it. The mouth is very narrow, hardly any valley at all, then it opens until it is probably a mile and a half or two miles wide, sloping toward the creek, down stream, not a steep slope, just a valley.

(Testimony of Joe McDonald.)

RECROSS EXAMINATION by Mr. Whitlock:

The pipeline I speak of comes into the stream just below the dam, and I have been told, is used by defendant, but I don't know of my own knowledge.

Thereupon, without objection, Exhibit 2 of the plaintiffs, a certified copy of the Rattlesnake Decree, Cause No. 1953, of the District Court of Missoula County, Montana, and Exhibit 4, the Registrar of Actions, in the same case, were offered and admitted as evidence. Exhibit 2 is identical with Exhibit A, made a part of the complaint heretofore copied at length in this transcript, except that the filing date as shown in Exhibit A attached to the complaint should be eliminated, and the same is therefore here [137] omitted.

(Testimony of Joe McDonald.)

EXHIBIT 4

is in words and figures as follows:

The Missoula Water Company,
a Corporation,

vs.

Charles E. Williams, Missoula County,
John E. Johnson, Elmer E. Hughes,
John White, Harry Mattison, and
others.

Injunction

Attorneys for Plaintiff:

Woody & Woody, Marshall & Stiff.

Attorneys for Defendants:

Gunn & Clayberg, W. P. Smith, Dixon &
Murphy.

Date	Proceedings	No.	Costs
August 13, 1901	Filed Complaint	1	\$ 5.00
" " "	Issued Summons handed T. C. M.		
" " "	Filed order for Injunction	2	
" " "	Filed Undertaking for Injunction and bond	3	
" " "	Issued Injunction, handed T.C.M.		
" 27, "	Filed Affidavit for Injunction against H. E. Day	4	
" " "	Filed Order for Injunction as to H. E. Day H. 132	5	
" " "	Issued Injunction handed Miss Nellie Fay		
" " "	Filed undertaking in Injunction as to H. E. Day (approved)	6	

(Testimony of Joe McDonald.)

Date	Proceedings	No.	Costs
Sept. 3, 1901	Filed Summons returned with service on the following: Elmer E. Hughes, Aug. 19th, Harry Mattison, Aug. 19th, Ollie D. Mattison, Aug. 19th, John Smith, Aug. 19th, B. F. Nesmith, Aug. 19th, Mary F. Nesmith, Aug. 19th, E. R. Kilburn, Aug. 19th, J. S. Kemp, Aug. 19th, Arthur Franklin, Aug. 19th, Thomas P. Street, Aug. 19th, R. M. Cobban, Aug. 19th, Peter Feddersohn, Aug. 19th, John E. Johnson, Aug. 20th, John White, Aug. 20th, Andrew Schilling, Aug. 20th, Delia Murray, Aug. 20th, Harvey Biggs, Aug. 20th, William Mattison, Aug. 20th, W. H. Raymond, Aug. 20th, J. W. Connelly, Aug. 20th, J. G. Ambrose, Aug. 20th, H. E. Day, Aug. 20th, William Neil, Aug. 20th, Mrs. E. J. Clements, Aug. 20th, C. H. Moss, Aug. 20th, L. W. Barrett, Aug. 20th, A. A. Settlamire, Aug. 20th, W. H. Hamilton, Aug. 20th, John Harkness, Aug. 20th, G. B. Frazier, Aug. 22nd, Charles E. Williams, Aug. 19th, W. P. Smith, Aug. 19, Theo LaChambre, Aug. 19, Sebastian Effinger, Aug. 19, Otto Quast, Aug. 20th, E. J. Wartman, Aug. 21st, F. L. Pelcher, Aug. 21, Cluff Vasser, 21, Joel A. Moss, Aug. 19, Geo. A. Duncan, Aug. 21, John Adams, Aug. 21, W. F. K. Beerkové, Aug. 21, C. E. Van Buren, Aug. 21, Chas. M. Owens, Aug. 26, John Capp, Aug. 28th.	7	

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(Testimony of Joe McDonald.)

	Date	Proceedings	No.	Costs
Sep.	24, 1901	Filed Demurrer	8	\$ 2.50
"	" "	Ordered that Defts attorneys show for whom they appear, and by what authority.		
Oct.	7, "	Demurrer set for hearing, Oct. 8, 1901		
"	8, "	Demurrer argued and submitted		
"	12, "	Genl Dem overruled, 2, 3, 8, Spl D. sustained, Pltf. granted 5 days to amend.		
"	17, "	Time for filing amend. complt extended 10 days from date.		
"	26, "	Filed amended complaint seal 10/17/33	9	.50
Nov.	14, "	Filed Demurrer to amended complt.	10	
"	25, "	Leave granted to withdraw de-demurrer filed Nov. 14 and to file amended demurrer.		
"	26, "	Order made Nov. 25th, 1901, vacated, General Demurrer allowed to stand.		
Dec.	13, "	Demurrer to amd. Compt set for hearing Saty. Dec. 14—10 A.M.		
"	14, "	Demurrer submitted without argument.		
"	16, "	Defendant withdraws motion, 25 days to answer.		
Jan.	10, 1902	Filed answer of H. C. Hollenbeck, Wallace P. Smith, Elmer E. Hughes, C. M. Owen, Anton Schilling, Mary F. Nesmith, Mamie E. Murray, Ollie D. Mattison, Amanda Mattison, Rufus Stryker, R. M. Cobban, J. G. Smith, A. E. Pound, Lucy Pound, H. C. Chattin, H. H. Hazelton, Adeline M.		

(Testimony of Joe McDonald.)

Date		Proceedings	No.	Costs
		Biggs, L. L. Wright, W. H. Raymont, Beadie Moss, C. H. Moss, F. M. Kilbourne, Thomas P. Street, A. B. Libby, W. A. Buswell, E. H. Sherman, G. B. Frazier, J. L. Johnson, John White and the County of Missoula	11	
Jan.	10, 1902	Filed separate answer of J. S. Kemp	12	
"	" "	Filed separate answer of William Neil	13	
"	" "	Filed separate answer Sebastian Effinger	14	
"	" "	Filed separate answer Peter Feddersohn	15	
"	" "	Filed separate answer of Otto Quast, C. E. Williams, Elmer E. Hughes, Ollie D. Mattison, Mary F. Nesmith, Jeanette Stilth, John White and John D. Johnson	16	
"	" "	Filed separate answer of W. R. Hamilton and H. E. Day	17	
"	" "	Filed separate answer of Charles E. Williams and Jennie Williams, Otto Quast and Jacob G. Ambrose seal 10/17/33	18	.50
"	" "	Filed separate answer of Missoula Lodge, No. 13, A. F. and A. M.	19	
"	" "	Filed separate answer of Theodore LaChambre	20	
"	" "	Filed separate answer of R. M. Cobban, W. H. Raymond, Charles E. Williams, William Neil, Jacob G. Ambrose, H. C. Chattin, John Barrett, E. J. Clements and John Capp	21	
Feb.	3, "	Stipulation to be filed		

(Testimony of Joe McDonald.)

	Date	Proceedings	No.	Costs
Feb.	4, 1902	Trial set for March 26th, 1902, at 10 A M		
Mar.	12, "	Filed stipulation to issue com- mission to take testimony	22	
"	" "	Filed Order to issue Commis- sion to take testimony	23	
"	" "	Issued Commission to take tes- timony of W. B. S. Higgins, handed Judge Woody	24	
"	14, "	Filed stipulation to issue commission to take testimony	25	
"	" "	Filed Order to issue Commis- sion to take testimony of Phil Shenon	26	
				[140]
Mar.	14, 1902	Issued Commission to take tes-) timony of Phil Shenon, handed) Judge Woody)	27	
"	21, "	Filed deposition of Phil Shenon)		
"	22, "	Filed deposition of W. B. S. Higgins	28	
"	24, "	Filed separate answer of Missoula Real Estate Assn.	29	
"	31, "	Filed amendment to plaintiff's amended Complaint	30	
"	" "	Filed petition in intervention of Philimine Fredline, admx.	31	
"	26, "	By agreement of counsel cause set for trial Monday, March 31st.		
"	31, "	Trial commenced.		
April	1, "	" continued		
"	2, "	" "		
"	" "	Filed affidavit of attendance of Wm. T. Hamilton	32	
"	" "	Filed affidavit of attendance of F. A. Hammond	33	
"	3, "	Received fee for Intervenor		\$ 5.00
"	" "	Receiver Stenographer fee for Intervenor		3.00

(Testimony of Joe McDonald.)

	Date	Proceedings	No.	Costs
April	3, 1902	Received Stenographer fee for Plaintiff		3.00
"	" "	Received fee Answer Missoula Real Estate Assn.		2.50
"	" "	Received fee for Gen. Separate Answers		25.00
"	4, "	Trial continued		
"	5, "	" "		
"	" "	Filed Subpoena	34	
"	8, "	" "	35	
"	8, "	Trial continues		
"	9, "	Filed subpoena of Winbu	36	
"	9, "	Trial continued		
				[141]
April	10, 1902	Trial Continued		
"	12, "	Trial continued to Wednesday, April 16th		
"	16, "	Trial resumed		
"	16, "	Received stenographers fees for 11 separate answers (3rd)		33.00
"	" "	Received stenographers fees for Missoula Real Estate Assn.		3.00
"	" "	Default, attached to back of amended complaint, entered for want of an answer of Harry Mattison, B. T. Nesmith, E. R. Kilburn, Harvey Biggs, J. W. Connelly, Wm. Mattison, A. A. Settlimier, John Harkness, Joel Moss, John Adams, C. E. Van Buren, E. J. Waitman, T. L. Pelcher and Cluff Vassar.		
"	18, "	Filed Reply to Separate answer of Feddersohn	37	
"	18, "	Filed Affidavit to Thos. C. Marshall	38	
"	19, "	Trial Continued to Monday April 21.		
"	21, "	Issued and filed Subpoena of H. C. Hollenbeck	39	

(Testimony of Joe McDonald.)

	Date	Proceedings	No.	Costs
Jan.	10, 1902	Issued Subpoena on Al Higgins	40	
"	" "	, " " " Peter		
		Feddersohn	41	
"	22, "	Filed notice of motion to file		
		complaint in intervention	42	
"	" "	Filed complaint in intervention		
		of Alvina Pelkey, et al.	43	5.00
"	" "	Stenographer Fee of Alvina		
		Pelkey et al.		3.00
"	21, "	Trial resumed		
"	21, "	Filed separate answer of George		
		Duncan	44	2.50
"	" "	Filed " " "		
		A. E. Franklin	45	2.50
"	" "	Filed " " "		
		Lucretia Worden et al.	46	
				[142]
April	21, 1902	Stenographer Fee Franklin \$3.00		
		and Duncan 3.00		6.00
"	" "	Further hearing on this cause		
		continued to May 6th, 1902		
May	6, "	Cause resumed and continued to		
		June 2nd, 1902		
June	2, "	Cause resumed and adjourned to		
		June 30th, 1902		
Sept.	4, 1902	Arguments made by plaintiffs		
		and defts. Attorneys		
July	18, 1903	Filed Notice of Motion for New		
		Trial	47	
"	25, 1903	Filed Exceptions	48	
Oct.	31, 1903	By consent plaintiff and defendants		
		are allowed to amend.		
"	" "	and motion for new trial is con-		
		tinued to Nov. 14th, 1903, 10 A. M.		
Dec.	5, 1903	Motion to amend complaint	49	
		Motion to amend Exceptions to		
"	" "	the Findings of Fact	50	
"	" "	Motion to Modify Decree	51	

(Testimony of Joe McDonald.)

	Date	Proceedings	No.	Costs
Dec.	5, 1903	Exceptions to Findings of Fact No. 6	52	
April	2, 1904	Motion to amend complaint set for hearing April 8th, 1904, at 10 A. M.		
July	11, 1904	Motion submitted without argument, Plaintiff to file a brief within 20 days if necessary.		
"	26, "	Filed and recorded Decree, Recorded Judg. Record H, Page 510		
"	" "	Filed affidavit for attachment against Charles E. Williams	53	\$ 2.50
"	" "	Filed Order granting citation H 522	54	
"	" "	Issued Order to show cause handed T. N. Marlowe	55	
"	28, "	Filed Petition for appointment of Commissioner	56	
				143]
July	28, 1904	Filed Order Appointing Commissioner H.522-523	57	
Aug.	4, 1904	Filed & recorded Extending time to prepare Bill of Exceptions, H.524	58	
Sept.	13, "	Filed Bill of Exceptions	59	
"	14, "	Filed Notice of Appeal	60	
"	" "	Filed and Recorded Undertaking on Appeal	61	
Oct.	11, "	Filed Report of Commissioner	62	
"	" "	" Order discharging Commissioner	63	
Jany.	3, 1905	Received fee for Certifying Transcript		5.00
"	13, "	Filed Petition for Appointment of Commissioner	64	
"	" "	Filed and Recorded Order Appointing Commissioner	65	
March	12, 1906	Certified Copy of Decree		3.50
July	23, "	Filed Petition for Appointment of Commissioner for 1906	66	
"	" "	Filed and Recorded Order appointing commissioner for 1906 I.162	67	
Oct.	20, 1906	Filed Commissioner's Report for 1906	68	

(Testimony of Joe McDonald.)

	Date	Proceedings	No.	Costs
July	17, 1908	Filed Affidavit etc.	69	
"	18, "	Filed Order citing Sebastian Effinger to appear	70	
"	21, "	Filed Order of Court	71	
Feb.	13, 1909	Seal		.50
July	21, 1910	Filed Petition for Appointment Water Com.	72	
"	" "	Filed Order Appointing Water Com.	73	
"	25, "	Filed Resignation Water Com.	74	
"	" "	Filed Order Appointing Water Com.	75	
[144]				
Jan.	14, 1910	Filed Report of Water Commissioner for 1910	76	
Aug.	18, 1911	Filed Petition for Appointment of Water Comm.	77	
"	" 1911	Filed Order Appointing & Oath of Office Rec. in Dok. K, 61	78	
July	27, 1911	Filed Report of Water Commissioner for 1911	79	
Aug.	5, 1913	Filed Petition for Appointment of Water Comm.	80	
"	6, "	Filed Order Appointing Comm. & Oath of Office	81	
"	9, "	Filed Affidavits charging W. R. Hamilton, Charles E. Day with Contempt of Court	82	
"	" "	Issued Order	83	
"	" "	Filed Order		
Jan.	10, 1914	Filed Notice of Hearing on Contempt	84	
Feb.	6, "	Filed Return of Hamilton & Day	85	
"	" "	" " " " " "	86	
"	7, "	Filed Notice of Intention to Apply for Commission to take Deposition of W. H. Raymond	87	
Mar.	3, "	Filed Deposition of W. H. Raymond	88	
"	20, "	Contempt proceedings set for hearing 3/30-14 10 A.M.		

(Testimony of Joe McDonald.)

	Date	Proceedings	No.	Costs
July	23, 1914	Filed Petition for App. of Water Comm. season of 1914	89	
"	25, "	Filed Order App. Lacy Taylor, Water Comm. season 1914	90	
"	31, "	Filed Resignation of Lacy Taylor, Water Comm.	91	
"	" "	Filed Order accepting resignation of Lacy Taylor	92	
"	" "	Filed Petition for App. of J. B. Pruden, Water Comm. season 1914	93	
				[145]
July	31, 1914	Filed Order Appointing J. B. Pruden, Water Comm. 1914	94	
July	17, 1915	Filed Petition to appoint J. M. Price, Water Comm. Season 1915	95	
"	" "	Filed Order App. J. M. Price Water Comm. season, 1915	96	
"	26, 1918	Filed affidavit and application for citation	97	
"	" "	Filed Order for citation	98	
"	" "	Issued Citation	99	
"	" "	Filed Citation		
Aug.	2, "	Filed Answer Geo. Likes	100	
"	2, "	Geo. Likes in Court answering to Order to show cause		
"	9, "	Geo. Likes fined \$1.00 for contempt. Fine paid Aug. 12th, 1918, Receipt #3168		\$ 1.00
July	17, 1919	Filed Petition for appointment of Water Commissioner	101	
"	19, "	Filed Order appointing Water Commissioner Judg. Rec. H. Page 625 Seal	102	.50
Nov.	1, "	Filed Water Commissioner's Report (1919)	103	
Aug.	3, 1920	Filed Petition for appointment of Water Com.	104	
"	" "	Filed Order appointing Water Commissioner Rec. Judg. Rec. "O" 335	105	

(Testimony of Joe McDonald.)

	Date	Proceedings	No.	Costs
Aug.	3, 1920	Filed Bond of Water Commissioner	106	
"	" "	Filed Oath of Water Commissioner	107	
"	27, "	Filed Report of Water Commissioner	108	
"	27, "	Filed Report of Water Commissioner Amended	109	
Aug.	8, 1921	Filed Bond of Water Commissioner	110	
"	8, "	Filed Order Appt. Water Commis- sioner Order Book G-7, pg. 84	111	
				[146]
Dec.	22, 1921	Filed Report of Water Commissioner	112	
"	22, "	Filed Order approving Water Commissioner's report	113	
Jan.	7, 1922	Filed Objections to Water Commissioner's report, etc.	114	
July	13, "	Filed Affidavit	115	
"	19, "	Filed Petition for Appoint- ment of Commissioner	116	
"	28, "	Filed Order Appointing Water Commis- sioner, Judg. P, page 283	117	
"	31, "	Filed Application for Citation	118	
"	31, "	Filed Order to Show Cause, Judg. Rec. P. page 285	119	
"	31, "	Issued Citation	120	
"	31, "	Filed Bond of Water Commissioner	121	
Aug.	1, "	Filed Citation	(120)	
"	7, "	Hearing on citation continued until Sept. 9, 1922		
"	25, "	Filed Water Commissioner's Report	122	
"	25, "	Filed Order approving Water Commissioner's Report, Judg. Rec. P. Page 304	123	
Sept.	9, "	Hearing on citation further continued until Sept. 11, 1922 at 9:30 A.M.		
"	11, "	On motion of counsel for de- fendant, E. J. S. Keen, Proceedings are ordered dismissed.		
"	12, "	Filed Memo. of costs and disbursements	124	

(Testimony of Joe McDonald.)

	Date	Proceedings	No.	Costs
Jan.	11, 1924	Filed Affidavit	125	
"	11, "	Issued Citation	126	
"	14, "	Filed Citation	(126)	
				[147]
Jan.	14, 1924	Citation directed against Chas. Rassman dismissed		
May	17, "	Filed Application for citation	127	
"	" "	Filed Order Judgment Record Q. page 449	128	
"	" "	Issued Citation	129	
"	24, "	Filed Citation	(129)	
"	28, "	Filed answer of W. F. and Jas. K. Hughes to answer	130	
"	28, "	Filed answer of Byron & Harry Hughes to answer	131	
"	28, "	Citation dismissed as to W. F. and James K. Hughes on motion of counsel for plft.		
"	28, "	By agreement of counsel, hearing on citation continued until June 30, 1924, pending of trial of cause #7883		
Aug.	1, "	Filed Petition	132	
"	1, "	Filed Order for Citation Judgment Record Q. page 514	133	
"	1, "	Issued Citation	134	
"	2, "	Filed Citation	(134)	
"	5, "	Filed Affidavit	135	
"	5, "	Filed Bond	136	
"	5, "	Filed Order	137	
"	5, "	Issued Injunction	138	
"	5, "	Filed Injunction	(138)	
"	8, "	Cause on trial Steno. fees		\$ 6.00
"	8, "	Upon Motion of atty. for Def. Tucker, Citation dismissed and Restraining Order Dissolved		
"	9, "	Filed Petition	139	
"	9, "	Filed Order appointing Water Commissioner, Judgment Record Q. page 524	140	

(Testimony of Joe McDonald.)

	Date	Proceedings	No.	Costs
Aug.	9, 1924	Filed Bond of Water Commissioner	141	
"	13, "	Filed Order dismissing Contempt Proceedings and Dissolving Injunction	142	
"	13, "	Filed Memorandum of costs and Disbursements	143	
"	14, "	Filed Motion to Retax cost & Notice of Motion	144	
Sept.	10, "	Filed report of Water Commissioner	145	
"	10, "	Filed Affidavit of Mailing	146	
Oct.	4, "	Filed Report of Water Commissioner	147	
"	4, "	Filed Order approving Report of Water Commissioner Order book G-8 page 111	148	
"	4, "	Filed Affidavit of Mailing	149	
"	22, "	Filed Protest of W. R. Hamilton to Comm. report filed Oct. 4, 1924	150	
Nov.	20, "	Plaintiffs motion to retax costs set for hearing Nov. 28, 1924, 9:30 A. M.		
"	20, "	Objections of W. R. Hamilton to Com. Water Report set for hearing Nov. 28, 1924 9:30 A.M.		
"	28, "	Motion to re-tax costs argued and submitted under advisement		
"	28, "	Protest of W. R. Hamilton submitted overruled		
Dec.	1, "	Filed Order approving Water Report	151	
"	1, "	Motion to re-tax costs sustained as to Attys. fees and Engineers services		
"	8, "	Filed order approving report of Water Commissioner	151	
July	20, 1925	Filed Petition	152	
"	20, "	Filed Order appointing Water Commissioner, Order Book G-8, pg. 303	153	
"	21, "	Filed Bond & Oath of Water Com. W. J. Teidt)	154	

(Testimony of Joe McDonald.)

	Date	Proceedings	No.	Costs
July	22, 1925	Filed Com. Report ending Aug. 21, 1925	155	
"	22, "	Filed Com. Report ending Aug. 31, 1925	156	
"	22, "	Filed Com. Report ending Sept. 15, 1925	157	
"	22, "	Filed Com. Report for season, 1925	158	
"	24, "	Filed affidavit of Mailing Notices	159	
"	29, "	Filed Protest of J. S. Kemp	160	
Oct.	19, "	Filed Order allowing fee of Water Commissioner	161	
June	5, 1926	Filed Petition for appointment of Water Com. for 1926	162	
"	9, "	Filed Petition for appointment of Water Com. for 1926	163	
"	12, "	Petitions heard, W. J. Teidt and Waldo Hunter appointed Water Coms.		
"	18, "	Filed Order appointing Water Commissioner for 1926, Order book G-8 page 543	164	
July	7, "	Filed Notice	165	
Dec.	16, "	Filed Water Report of Water Commissioners for 1926	166	
"	17, "	Filed affidavit of Mailing.		
Jan.	5, 1927	Filed protest of L. E. Tucker, et al.	166½	
"	24, "	Filed Order fixing time of hearing Protests	167	
"	26, "	Filed Order with Sheriff's return	167½	
May	14, "	Filed Order fixing fees and compensation Order Book G-9, pg. 186	168	
July	14, "	Filed Petition for Appointment of Water Commissioner	169	
"	23, "	Filed Proof of Publication	170	
Aug.	2, "	Filed Order appointing Water Commissioner for 1927, Order book G-9, page 251	171	
Aug.	2, 1927	Filed Bond	172	
Oct.	15, "	Filed Report of Water Commissioner	173 & 173½	
"	18, "	Filed Affidavit of Mailing Notices	174	
Nov.	14, "	Filed Order Fixing fees and compensation Or. Book G-9 page 319	175	

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(Testimony of Joe McDonald.)

	Date	Proceedings	No.	Costs
July	30, 1928	Filed Petition for appointment of Water Comm. 1928	176	
"	31, "	Filed Order appointing Water Commissioner Od. Bk. G-9, pg. 460	177	
Aug.	4, "	Filed Bond of Water Commissioner	178	
Oct.	11, "	Filed Report of Water Commissioner (1928)	179	
Nov.	9, "	Filed Affidavit of Mailing Water Notices	181	
"	14, "	Filed Order fixing compensation of Water Com. Od. Bk. G-9 528	182	
July	5, 1929	Filed Petition for appointment of Water Com.—1929	183	
"	11, "	Filed Order appointing Water Commissioner. Od. Bk. G-10 pg. 102	184	
"	16, "	Filed Oath of Office	185	
"	17, "	Order appointing Water Commissioner modified, bond \$1500.00 instead of \$2000.00		
"	17, "	Filed bond of Water Commissioner	186	
Oct.	7, "	Filed report of Water Commissioner	187	
"	7, "	Filed affidavit of Mailing Notices	188	
"	21, "	Filed Motion to Retax 1929 Com. Salary—L. E. Tucker	189	
"	21, "	Filed Motion to Retax 1929 Com. Salary—J. C. Sain	190	
"	30, "	Filed Order Fixing day of hearing Protest of L. E. Tucker, Or. Book G-10—234	191	
Nov.	5, 1929	Filed Praecipe for subpoena	192	
"	5, "	Issued Subpoena	193	
"	6, "	Motions of L. E. Tucker and J. C. Sain on for hearing and dismissed on Motion of Atty. for Protesters.		
"	7, "	Filed Order fixing fees of Water Com. Or. Book G-10 pg. 271	194	

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(Testimony of Joe McDonald.)

	Date	Proceedings	No.	Costs
July	10, 1930	Filed Petition for appointment of Water Commissioner	195	
"	10, "	Filed Order appointing Water Commissioner	196	
"	12, "	Filed Bond and Oath of Office of Water Commissioner	197	
Aug.	11, "	Issued Execution (J. C. Sain)	198	\$ 1.00
"	14, "	Filed Execution fully satisfied		
Sept.	26, "	Filed Report of Water Commissioner	199	
"	26, "	Filed Affidavit of Mailing Notices	200	
Oct.	23, "	Filed Order fixing fees of Water Com.	201	
Dec.	20, "	Issued Execution on Ed Ray	202	1.00
"	20, "	Filed Execution fully satisfied (See Water Report 1930)	202	
June	29, 1931	Filed Petition for appointment of Water Commissioner	203	
"	29, "	Filed Order appointing Water Commissioner	204	
July	3, "	Filed Bond of Water Commissioner	205	
Sept.	15, "	Filed Order Discharging Water Commissioner Or. Book G-10 pg. 556	206	
"	16, "	Filed Report of Water Commissioner	207	
Oct.	9, "	Filed Order fixing fees of Water Com.	208	
July	30, 1932	Filed Petition for Appointment of Water Com.	209	
				[152]
July	30, 1932	Filed Order Appointing Water Water Commissioner	210	
Aug.	9, "	Filed Petition for discharging Water Commissioner etc.	211	
"	9, "	Filed Order for hearing on Petition	212	
"	15, "	Filed Notice of hearing and affidavit of service	213	
"	15, "	Cause heard Petition denied		
"	16, "	Filed Bond of Water Commissioner	214	
Sept.	10, "	Filed Report of W. J. Tiedt Water Com., 1932	215	
Oct.	5, "	Filed Order Fixing Fees & Com. of Water Com.	216	

(Testimony of Joe McDonald.)

	Date	Proceedings	No.	Costs
July	29, 1933	Filed Petition for Appointment	217	
"	29, "	Filed Order appointing Water Commissioner	218	
"	29, "	Filed Bond of Water Commissioner Bond Book 101, page 105	219	
Oct.	2, "	Filed Report of Arthur Sticht, Water Com., 1933	220	
"	3, "	Filed Petition for increase of Water Com's Salary	221	
"	3, "	Filed Order Fixing Fees of Water Com.	222	
Nov.	3, "	Filed Order Fixing Fees of Water Com.	223	
(Duly Certified)				

As to Exhibit 3, and for the purpose of shortening the record, it is agreed in open court between the respective counsel that the same shows a judgment of date of February 15, 1932, entered in the District Court of Missoula County, Montana in an action wherein J. N. Boles and others were plaintiffs and Charles Martinson and others were defendants, Cause #11818 [153] of that court, in which the relative and various interests of the appropriators of Rattlesnake creek, so far as applicable to the water diverted through the Hollenbeck ditch, were adjudicated and determined, and those relative interests are as set out in Exhibit 3, now offered and admitted in evidence. The same, so far as material in this case, being set out in Findings of Fact II and VI of the Findings of Fact in said case; the same being in words and figures as follows:

(Testimony of Joe McDonald.)

II.

That a decree was duly given and made on July 9, 1903 by this court in an action wherein The Missoula Water Company, a corporation, was the plaintiff and Charles E. Williams, et al were the defendants; and said action was designated as No. 1953, which decree found and determined by Finding of Fact No. 10

“That the defendants H. C. Hollenbeck, Wallace P. Smith, Elmer E. Hughes, C. M. Owen, Emma Shilling, Mary F. Nesmith, Mamie E. Murray, Ollie D. Madison, Amanda Pound, H. C. Chattin, H. Hazleton, Adeline C. Briggs, Della T. Wright, Carrie B. Raymond, Beadie Moss, C. H. Moss, Effie M. Kilbourne, Thomas P. Street, A. H. Libby, W. A. Buzzwell, Mrs. E. H. Sherman, J. B. Frazier, J. E. Johnson, John White and Missoula County, by their predecessors in interest August 28, 1882, made an appropriation of (145) one hundred forty-five inches of the water of said Rattlesnake Creek by what is called the Hollenbeck Ditch, conducting water to the Hollenbeck Homestead.”

and said decree also found and determined by Finding of Fact No. 16 that the

same defendants made an additional appropriation of 50 inches by an extension of the said Hollenbeck Ditch to what is called the Daily Pre-emption Claim on July 1, 1888.

(Testimony of Joe McDonald.)

That by said decree it was concluded as a matter of law that the said defendants were entitled to the use and enjoyment of the one hundred forty-five (145) inches of water of Rattlesnake Creek, statutory measurement, of date August 28, 1882, and fifty (50) inches of date of July 1, 1888. [154]

VI.

That the rights of the plaintiffs and defendants, as tenants in common, respecting the use and division of the water flowing in said Hollenbeck Ditch is determined and fixed as follows, to wit:

Parties	Acreage	Quantity of Water
Lilian L. Boles	2.00	3.136
H. E. Sturm	2.50	3.95
W. M. Russell	1.50	2.352
Minnie E. Seeley	.50	.784
Loretta M. Smith	3.00	4.704
N. S. Lilly	3.75	5.86
W. J. Johnson	1.90	2.959
Inez E. Jackman	2.10	3.272
A. M. Rogers	2.75	4.332
Frank E. Smith	1.12	1.756
R. H. Miller	5.00	7.84
Orpha Miller Talbot	2.50	3.92
Constance E. Baker	2.00	3.136
Rose I. Downey	5.50	8.624
E. E. Warner & D. W. Warner	4.50	7.056
C. W. Leapheart	4.50	7.056
Chas. Rossman & P. Rossman	2.00	3.136

(Testimony of Joe McDonald.)

G. M. Reeves	1.50	2.352
Horace Green	1.00	1.568
John R. Day	1.00	1.568
Lulu O. Wohlschlager	2.25	3.563
A. L. Kagle	2.25	3.563
W. T. Burnett	2.00	3.136
Mamie V. Weir	1.00	1.568
Albert Free & Sam Mercer	1.75	2.74
E. C. Lucas & A. E. Bristow	1.25	1.96
E. R. Janes	.90	1.41
Agathy Brown	6.00	9.40
E. F. Roth	10.00	15.68
Missoula County	32.00	36.00
Tennie E. Greenough	10.114	15.85
Charles Hart	1.612	2.52
Frank A. Graehl	.912	1.43
Carl Peterson & Miss C. C.	10.73	16.82

Totals

133.388 A. 195.000''

Plaintiffs' Exhibit 3 as admitted for the limited purpose of showing the relative rights and interests of various plaintiffs in Right No. 10 and Right No. 16 of the Rattlesnake decree, Cause #1953.

C. W. LEAPHART, [155]

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is C. W. Leaphart; I live up the Rattlesnake; I am Dean of the Law School of the University of Montana at Missoula. I irrigate, like any other farmer, a small tract of land, and have water from the Hollenbeck Ditch. My relative interest in the Hollenbeck Ditch was determined in the decree Cause #11818, just introduced in evidence. I have resided up there since 1921, and have helped make observations of Rattlesnake creek water flow in the last few years. The first measurement, in which I participated was July 15, 1926. Others participated with me. We measured the water flow at the head of the Mill Ditch right under the streetcar track, through a ten foot weir.

Q. And what was the result of your measurement there?

Mr. WHITLOCK: That is objected to as referring to a time not material.

The COURT: Overruled.

Mr. WHITLOCK: Exception.

The measurement was taken at 5:45 in the evening and there was 4 and seven eighths inches depth of water going over the weir. I went up the stream to note the condition of the stream flow above the weir and there was no water coming over the dam. The water commissioner on the stream had shut the dam, so that no water was coming over. There was

(Testimony of C. W. Leaphart.)

then water flowing in the Fredline ditch. I made no further note of the stream condition at that time. There is always water flowing in the Fredline ditch. I have seen it every day, and never saw it dry. [156]

The water going through the weir where we measured was going into the Missoula river and the water in the Fredline ditch was going to the Hughes Brothers' gardens. During the years I have lived on Rattlesnake I have observed the relative flow during the summer months above the head of the Mill ditch. I go over it almost every day, and there is always water flowing to the Missoula river there through the mouth of Rattlesnake. I would estimate the amount as being about the same as that measured. I made other measurements at the same place on July 16th, 18th and 20th, and August 3rd of 1926.

Q. Will you give those measurements?

Mr. WHITLOCK: The same objection.

The COURT: Overruled.

Mr. WHITLOCK: Exception.

The result on July 16th, 18th and 20th was practically the same as July 15, roughly four and a half inches; on August 3rd, there was two and a quarter inches. I did not observe the stream condition above on all occasions, but upon at least one other I noted that the dam was shut down completely. Being asked as to what extent the agricultural rights are used, eliminating from consideration the rights of the Water Company, of course in the summer time when the water is getting short they use

(Testimony of C. W. Leaphart.)

all of it—all they can get. I have observed what happens when they are irrigating heavily above. In the year of Mr. Tucker's suit against the Water Company I noticed especially this fact or the year following, he irrigated very heavily and the result was drowning out the crops on that bench just below the bench I am on. It is about ten or twenty feet lower maybe in the neighborhood of the Howard Grocery. I have not observed as to the extent of the flow of the stream down near the head of the Mill ditch when they are irrigating heavily above.

CROSS EXAMINATION by Mr. Whitlock:

I acquired my property in 1921, and know nothing of water use on Rattlesnake prior to that date. The dam and diversion works of the defendant were constructed when I went up there, and the city supply was then being taken at the point where it is now taken. There was four and seven eighths inches depth of water on the weir at the time I measured on July 15, 1926, and four and a half on the 16th, 18th [157] and on the 20th, but on August 3rd, the amount had gone down to two and a quarter inches.

GEORGE CROMWELL,

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is George Cromwell; I am a farmer living on Rattlesnake. I irrigate six acres from Rattle-

(Testimony of George Cromwell.)

snake. The land is known as the Nellie Sticht land. I have a life lease on it from Glen Sticht, who was the successor of Janet Sticht, who was a party to the decree. I take the water out of the Otto Quast ditch, No. 20, six inches. In July, 1931 my water was shut off and I was unable to get any more water that year, and suffered a complete crop failure for want of water. I gave up my own crop and worked out. 1932 was fair as to water, and this year I have had water. 1931 was an unprecedentedly dry year. I took possession of my land in January, 1931.

Thereupon it was agreed in open court between the respective counsel, concerning the land holdings and water rights of each of the other plaintiffs in this action, who have not yet been called as witnesses, they would testify as to their respective rights:

(a) That they all acquired their interest up there subsequent to the decree in Cause #1953, except Missoula County, who was a party to the decree in Cause #1953;

(b) That they are respective successors in interest to the parties in the decree in Cause #1953;

(c) That they severally own the lands which they alleged in the complaint to own, and that the lands require [158] water for irrigation to be profitably farmed.

L. E. TUCKER,

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is L. E. Tucker. I reside in Los Angeles at the present time, but I did reside on Rattlesnake creek formerly. I owned land on Rattlesnake creek in 1910 or 1911, but in 1921, I acquired what is known as the Quast ranch, now in the possession of Joe McDonald, who preceded me as a witness here. In the possession of the Quast ranch from 1921 until my occupancy ceased, I had 45 inches in right 5; 40 inches in right 10; 220½ in right 20; and 56 and 8/10 in right 21 of Cause #1953, with which I irrigated approximately 170 acres. I began my occupancy of the Quast ranch in September, 1921, and stayed until October, 1929. During that period I made observations and measurements on Rattlesnake creek. I was present on August 7, 1924, when Mr. Ray, who testified here, made measurements of Rattlesnake stream flow. His measurements were made at my instance.

A. Yes sir.

Mr. WHITLOCK: That is objected to as not material in point of time.

The COURT: Overruled.

Mr. WHITLOCK: Exception.

A. 1640.8 inches.

That represented the entire flow of the stream, measured at four different points. During the seven

(Testimony of L. E. Tucker.)

or eight years that I was a user of Rattlesnake creek water, I observed the low water period, which was around August 7th, 10th or 15th. [159] The stream flow on August 7, 1924 was approximately the same as upon the same date of each of the other years. I never measured under 1600 miners inches of water in the stream.

I recall a measurement at a weir near the head of the Mill ditch in August, 1926. The weir was installed in Rattlesnake creek at the head of the Mill ditch by me with some help from my neighbors. It was a 10 foot weir, and we measured the water flowing through it every day for 30 days, sometimes in the morning and sometimes in the afternoon; that was in 1926, the first measurement being July 15, 1926. I observed the condition of stream flow higher up between this weir and up to the dam. The stream would be dry in places along that stretch, and some places would be more flow, and places there was water along the stream. Below the dam there was generally a little water going over the chute, sometimes it would be perfectly dry, but generally a little water wasting over. The bedrock varies on the stream, and the water raised with the bedrock; sometimes water would be exposed in the gravel in pools, and then, again, a hundred yards to 300 yards below the dam, the channel would be almost dry and you would find a place where there would be a little pool, and so on down clear to the city park, the Greenough park. The Hollenbeck ditch always had

(Testimony of L. E. Tucker.)

water; they could put a little dam out in the stream and catch all the seepage water and spring water, and there would probably be 35 or 40 inches for the Hollenbeck ditch. When we would have no irrigation above, that conditions would exist when there would be no water coming over the dam, or very little water, and the stream bed just below the dam would generally be dry. At the time when water was low and we needed water [160] the stream below the dam, as a rule, was dry—a very little running water for a short distance. There was some seepage water coming through in under the dam when the old dam was in, and we had more water, and we had more water then than after the new dam was put in, in 1924; I am not sure of the exact time. This dry condition of the stream bed continued down the stream to Greenough park, which is probably half a mile or three quarters above the road where I had installed the weir at the head of the Mill ditch. From the Greenough park down, there was mostly always some flow probably, some places the flow would be light, and some places heavy. At the bridge where the road crosses the Rattlesnake, you would generally see three or four hundred yards above the weir, and you could see a couple of hundred inches of water there. I don't think I ever saw it anywhere near dry. From there on down there would be some places where there would be considerable more water. Where the Fredline ditch came out, there was generally plenty of water com-

(Testimony of L. E. Tucker.)

ing out, by plenty of water, I mean probably five or six hundred inches. I never measured the water at that place. The water flowing in the stream at the head of the Fredline ditch came from seepage water through the banks of the stream and water that would raise in the bottom of the stream. There are no tributaries coming in from the sides. Eliminating the water used and claimed by the Water Company each year while I was on the stream we, meaning agricultural rights, used practically all the water we could get in low water—when the water was scarce in the stream, I would say all the decreed agricultural rights as far as there was water to supply them.

CROSS EXAMINATION by Mr. Whitlock:

My observation of Rattlesnake creek water rights does not date earlier than 1921. I said I made observations [161] of the stream flow below the dam and found some places where there was water and then further down a place where there wasn't so much, and then striking a place where there was a little more, and I usually observed some water flowing down where the bridge crosses the creek, which is close to town; that is on Cherry Street, I believe they call it, say about 300 yards above where the weir was in.

REDIRECT EXAMINATION by Mr. Wilson:

Q. I don't believe I asked you how much water was flowing through the weir whenever you made

(Testimony of L. E. Tucker.)

measurements, did I?

A. No sir, you didn't.

Q. Well, will you state?

Mr. WHITLOCK: That is objected to as not material as to time.

The COURT: Overruled.

Mr. WHITLOCK: Exception.

The COURT: Answer, Witness.

I had notes on the measurement, but I haven't the notes here. I remember our first measurement very well and several others. On July 15, 1926, we measured; there was a little more than four and a half inches depth of water on the weir. In setting the weir, a pool is formed up stream from the weir for about 15 feet, and a peg is driven level with the weir top and back far enough to be away from the break of the water, and we measured the water depth from the top of this peg, to determine the depth of water flowing over the weir and there was slightly more than four and a half inches at 4:00 in the afternoon when we measured it. The least I ever measured at any time was in the latter part of the measurements; along about the 5th, 6th or 10th of [162] August. Along in there it got down; one measurement I made in the afternoon was about three and three quarters inches; in the morning we had five inches at that time. At different times it would vary. I think the least I ever measured was three and three quarters and the most I ever measured was seven and a half

(Testimony of L. E. Tucker.)

inches going over the weir. The condition during those times of the stream bed below the dam, after about the 15th or 20th of July, there was never much difference as to the condition of the stream, because then about the water would all be taken out; that was in the stream. Sometimes when we had plenty of irrigation on the bench, the water would flow in the stream above the city park, and I have seen quite a bit of water flow in when we had plenty of water to irrigate. I never saw the Fredline ditch dry, only in the winter time when they turned the water out. There was always plenty of water there.

RECROSS EXAMINATION by Mr. Whitlock:

The water declined during the latter part of the measurements. It was the lightest about August 15th, running about an inch lighter on the 15th of August than on the 15th of July. My last measurement was about the 15th of August. It varied with the different time of the day you measured. In the morning you would get considerable more flow than in the afternoon. I was not present when Mr. Leaphart made his measurement.

ED NEWTON,

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is Ed Newton; I reside in Missoula and con- [163] duct a cabinet shop by occupation. I have lived in Missoula 43 years. I know the Mill ditch out of Rattlesnake creek. When I first came to Missoula, I lived right close to the head-gate. I used the ditch then for power in my shop, beginning in 1903 or 1904, somewhere in there. Prior to that time I had my home near the head of the ditch. The water ceased being used through the Mill ditch, as near as I can remember, either in the fall of 1905 or spring of 1906, I wouldn't be sure.

While it was used, the Mill ditch was used for a water wheel for power on Higgins Avenue; and when I say that the use ceased in the fall of 1905 or spring of 1906, I tie my recollection to the following incident:

I moved from there to the other shop that I built in 1907, and I used a motor then, electric power, because the water was shut off, and I used the water power from the water in the ditch until it was shut off, when I began to use the electric power. The mill for which the Mill ditch was used was a flour mill, and such use was prior to my use, which was a lumber mill and cabinet shop, which I conducted

(Testimony of Ed Newton.)

in the old flour mill. I did not know the ditch when it was used for flour mill purposes.

CROSS EXAMINATION by Mr. Whitlock:

When I used the Mill ditch for my cabinet shop, I was the only person on the ditch that would use it, and my use was discontinued in the fall of 1905 or in the spring of 1906. Prior to that time the use of the ditch had gradually declined to some extent. There wasn't as much water when I last used it as when I first used it.

WALTER M. HAY, [164]

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is Walter M. Hay; I reside in Missoula; my occupation is carpenter shop foreman. I have lived in Missoula more than 45 years and have seen the Mill ditch off and on ever since I came there. My first acquaintance with the ditch was in making repairs. A good bit of it carried in flume and that would get out of repair and I have repaired it. The use made of the ditch was to run the water wheel down at the old Mill plant. I worked in Mr. Newton's cabinet shop after it was started there. The ditch was first used for a flour mill, and for a number of years, no use was made of it until Mr.

(Testimony of Walter M. Hay.)

Newton's cabinet shop was opened in the old flour mill, when it was used to run his machines and I worked for him. The use ceased in the fall of 1905 or spring of 1906.

CROSS EXAMINATION by Mr. Whitlock:

Prior to Mr. Newton's cabinet shop going into the old flour mill there was a good many years when no use was made at all of the water through the Mill ditch, and then the water was used to run the machinery in the cabinet shop of Mr. Newton. There wasn't a great quantity of water, still it took considerable to drive the wheel. There was supposed to be flow enough to keep the penstock filled up. The flow kept working down, getting a little less all the time. We had to wait at times for the penstock to fill up, but that was very seldom, and in the fall of 1905, I think, motor power use commenced and the water power ceased.

HENRY BERGSTROM, [165]

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is Henry Bergstrom; I live in Missoula, and my occupation is cabinet shop employee for Mr. Newton. I have lived in Missoula about 30 years. I know the Mill ditch. My best recollection

(Testimony of Henry Bergstrom.)

is that the Mill ditch ceased to be used for the flowing of water in the fall of 1905 or spring of 1906. I have this recollection or acquaintance with the ditch: I went to work for Mr. Newton in the spring of 1905, and we used the water that year for water power.

JOHN J. FLYNN,

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is John J. Flynn; I reside four miles west of Missoula and have lived in the vicinity of Missoula all my life.

I have known Mill ditch since I was a little boy. My offhand opinion is that the water ceased to be used in the Mill ditch in 1905, but I wouldn't say definitely. I mention this incident in connection with the later use of the Mill ditch, that is definitely fixed: My brother had a boy drowned in the ditch in 1903 in October, and necessarily there was then water flowing in the ditch. The ditch was closed, I thought, about a year or two after that—a couple of years after that. I couldn't say definitely.

HENRY PARTOLL,

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows: [166]

DIRECT EXAMINATION by Mr. Wilson:

My name is Henry Partoll; I reside in Missoula, and have lived here for 43 years. I know the original Higgins ditch; I live in the near neighborhood or vicinity of that ditch and remember when water flowed through the Higgins ditch. I remember of water flowing about 1908 or 1909. By 1908 or 1909, I mean there was water in the ditch yet. I paid no attention to the first time I saw water in the ditch, but afterwards, in 1898, I bought ground there in block Q, and there were eight lots I bought, and then the ditch ran right through the lots; and then afterwards the ditch was taken around the corner off the lots, and in front of the sidewalk; that is the first attention I paid to the ditch. This ground was in Higgins Addition to Missoula, in block Q, on Spruce Street. It was still flowing in 1904, the full stream. My brother was out here, and he asked me where the water came from. That was in 1904. I think it flowed until 1909, and the water was used for irrigation west of town.

CROSS EXAMINATION by Mr. Pope:

A child got drowned on Front Street and my wife was so anxious of our child to get in there, that in 1906 I drove stakes so that the children couldn't

(Testimony of Henry Partoll.)

get under the bridge. The ditch was then right there across the street.

REDIRECT EXAMINATION by Mr. Wilson:

The boys that we were worried about, that made me drive the stakes were my two children. I had two small children. This boy, Albert, was born in 1904, and he is one of the children I was concerned about, when I drove the stakes in front of the ditch, and I had another child besides that, [167] born in 1903.

JOHN A. MORRELLIS,

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is John A. Morrellis; I live in Missoula and have lived here for thirty-four years. The photograph, which you hand me, was taken at my home, and the stream of water shown in the photograph is the Mill ditch. The cart "transfer" was my wagon and that is me in the wagon. The picture was taken in 1904. The scene on the Mill ditch, represented by the picture, is on Cedar Street in Missoula.

Picture offered and admitted in evidence.

J. C. SAIN,

called as a witness on behalf of plaintiffs, recalled for further examination, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

When I came to Missoula in 1903, water was then flowing in the original Higgins ditch. I cannot remember how long after it continued, but that was my first year in Missoula vicinity, and it was then flowing.

CHARLES E. QUAST,

called as a witness on behalf of plaintiffs and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My name is Charles E. Quast. I live up Grant Creek near Missoula, and I am by occupation a dairyman.

I did live on Rattlesnake Creek from 1894 until 1920 or 1921, and was dairying on Rattlesnake creek. First I worked for my brother, Otto, and afterwards I had the [168] Peter Fedderson and Charlie Williams places. Otto was my brother and he occupied the land now occupied by Joe McDonald.

When I worked for him, I observed the extent of his irrigation, and he had all the water he wanted to irrigate with; and that was the case over a period of about seven or eight years, when I worked for him. After that, I occupied the Peter Fedderson and Charlie Williams places.

PLAINTIFFS REST.

[169]

DEFENDANT'S CASE IN CHIEF.

DEFENDANT'S TESTIMONY.

H. S. THANE,

called as a witness on behalf of defendant and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Whitlock:

My name is H. S. Thane. My occupation, civil engineer. I am superintendent of Missoula division of Montana Power Company. I have had twenty-four or twenty-five years of study and experience, and have been employed by the Montana Power Company and its predecessors since 1910, and have been familiar with the system since then, and in charge of it since 1920. During my connection with that system, I have had occasion to observe the use and distribution of the water of Rattlesnake creek, and the flow of the stream both above and below the point of diversion. The water is diverted to supply the city of Missoula, at a point about three miles north of town.

I have prepared a map at the request of defendant's attorneys, showing the ditches and other points of interest on Rattlesnake creek.

The map is offered and admitted in evidence without objection as defendant's exhibit 6. [Original exhibit in custody of clerk]

The point where the water is diverted by defendant for the city of Missoula is marked "dam" on the map, and is situated near the center of Section 2. The intake of the old Higgins ditch was at

(Testimony of H. S. Thane.)

a point where the creek crosses the side line of section 11, and the old Mill ditch is somewhere between Broadway Street in Missoula and the Northern Pacific tracks. There is no particular designation of that on the map, [170] but it is slightly above East Pine Street, and within 100 yards of East Pine Street. It is a little over three miles from the "dam" to the Missoula River, which is the larger stream on the map, into which Rattlesnake creek flows. It is about three miles from the "dam" to the head of the old Mill ditch and about two miles from the "dam" to the head of the Higgins ditch. The scale of the map is 800 feet to the inch. The point of prior diversion made to serve Missoula prior to the present location of the "dam" is marked on the map "water works". The change of point of diversion from the point marked "water works" to the "dam" was made before I became familiar with the stream.

I am familiar with the chain of title to the "water works" system and the water rights now used and claimed by Montana Power. I briefly state the same giving dates starting back at the beginning: Frank L. Worden and wife and C. P. Higgins and wife to Missoula Water Works and Milling Company, December 31st, 1885, covering the water system, mill and water rights. The next transfer is from the C. P. Higgins estate to Missoula Water Works and Milling Company, covering the Higgins right, on October 22nd, 1895. The next is a transfer

(Testimony of H. S. Thane.)

from the Missoula Water Works and Milling Company by their change of name to Missoula Water Company, a Montana corporation, on November 2nd, 1895. Missoula Water Company, a Montana corporation, to the Missoula Water Company, an Oregon corporation, through Cornelius Sullivan, Trustee, on February 7th, 1898. The Missoula Water Company, an Oregon corporation, to Missoula Light & Water Company, an Oregon corporation, through John M. Keith, Trustee, on January 28th, 1904. Missoula Light & Water Company, an Oregon corporation, to Mis- [171] soula Light & Water Company, a Washington corporation, on September 18th, 1906. Missoula Light & Water Company to Missoula Public Service Company, on October 31st, 1924. Missoula Public Service Company to the Montana Power Company on October 31st, 1929.

The Montana Power Company is the present owner and defendant in this action. The Clark interests in the chain of title above were the Missoula Light and Power Company of Washington and the Missoula Public Service Company.

I have examined the decree in Cause #1953, previously introduced in evidence here, and I here list the rights given to Missoula Water Company, the plaintiff in that case, that are by number, amount and date as follows:

(Testimony of H. S. Thane.)

Number	Amount	Date
1	946 inches	1866
2	160 “	1868
3	131½ “	1871
4 (Part of)	65 “	1871
8	461½ “	1881
9	348 “	1881
14	645 “	1887

Since the decree, defendant and its predecessors have acquired the additional decreed rights:

Number	Amount	Date
5 (Part of)	115 inches	1872
11	130 “	1882
19	50 “	1892
20	65 “	1895
21	142 “	1895

Montana Power Company is now the owner of the system and water rights as I have described. I have prepared a chart, which correctly shows the relative position and location on the stream of the several rights claimed by plaintiffs in this case, and those claimed by the defendant. It is diagrammatic; the plat indicates by name the rights both [172] of defendant and all of the plaintiffs, who appear in this action.

Mr. WHITLOCK: We offer the chart, Exhibit 7, in evidence.

Mr. WILSON: We object to this, if your Honor please, as a conclusion of the witness and not testi-

(Testimony of H. S. Thane.)

mony of any fact in the case; and as to the location on the stream of the rights that is the subject in issue which must necessarily be determined by the Court.

The COURT: It may be introduced for what it is worth.

Mr. WILSON: Exception.

[Original exhibit in custody of clerk]

The red letters and figures indicate the rights which we claim to divert at the "dam", but are temporarily diverting in ditches, and they are listed under the various ditches and underlined in red. The same rights have a red line under them at their other points of use.

Describing the water system of defendant, the same consists of eight lake reservoirs—storage reservoirs at the head of the Rattlesnake in the mountains, a concrete diverting dam and settling basin which is located on the map here, and a 30-inch wood stave pipe 17,000 feet long leading to a reservoir on the hill—a 1,000,000 gallon concrete reservoir, and approximately 67 miles of distribution system ranging in size from 24-inch to two-inch.

Of my personal knowledge that system has been used to furnish Missoula since 1910, and there is no other system furnishing water to Missoula and its inhabitants, except a small private system that serves half a dozen customers. The head of the Mill

(Testimony of H. S. Thane.)

ditch is lower in elevation than most of the land in the city of Missoula and water could not be furnished [173] to the City of Missoula by gravity from that point. I have charge of the distribution of water through defendant's system and know what rights defendant claims to use in furnishing the city. Defendant uses all of its rights to furnish the city to the extent needed, and I have kept records of the waters used through the system over a long period of time. The measurements are determined by a Venturi meter located on the hill. It operates in a way that it makes a chart showing the amount used and I have the original of such charts here in court, from which I have prepared a table showing the maximum and minimum flow over a period of years (which table is produced by the witness). The table starts in 1905 and ends with 1933 and is shown in two sheets, which are offered in evidence as defendant's Exhibit 8, and correctly reports the amount of water as shown thereon for the period shown thereon.

Mr. WHITLOCK: We offer this, Defendant's Exhibit 8, in evidence.

Mr. WILSON: It is objected to upon the ground that it is immaterial, the right to the use of water not being in this case determined by the use which may have been made by the defendant, nor will the use which will be permitted in the future be determined by the use which may have been made heretofore.

(Testimony of H. S. Thane.)

The COURT: What is this supposed to represent, Mr. Whitlock?

Mr. WHITLOCK: The amount of water actually used by the Montana Power Company, the defendant, and its predecessors, in this case, extending over a [174] period of years from 1905 down to 1933.

The COURT: You mean the amount distributed?

Mr. WHITLOCK: Yes, your Honor; taken out of this stream at the dam as now located.

The COURT: Where did you measure it?

A. That is measured in the pipe—at a point in the 30-inch pipe.

The COURT: Where it leaves the dam?

A. Somewhere in that pipe, yes sir.

The COURT: That leads from the dam?

A. That leads from the dam, yes sir.

The COURT: I doubt if you find it material, but it may be introduced in evidence and in so far as entitled to no consideration the Court will give it none in making up its decision. For the sake of the record, overruled. [175]

(Testimony of H. S. Thane.)

EXHIBIT NO. 8.

WATER SYSTEM CONSUMPTION

Average Miner's Inches per day—From available records

						<i>Source</i>	
1905	November	309	(Max. 371	Min. 270)		Venturi Charts	
1907	January	300	"	371	" 247	"	"
1908	February	371	"	433	" 340	"	"
	March	340	"	371	" 309	"	"
	April	371	"	495	" 247	"	"
	June	525	"	680	" 433	"	"
	November	309	"	433	" 247	"	"
1909	July	680	"	990	" 433	"	"
	August	680	"	928	" 433	"	"
	September	618	"	742	" 494	"	"
1910	July	495	"	742	" 371	"	"
	August	565	"	742	" 371	"	"
1911	July	520	"	803	" 371	"	"
	August	520	"	742	" 309	"	"
1912	June	519	"	680	" 309	"	"
	July	556	"	927	" 371	"	"
1913	June	560	"	1050	" 371	"	"
1914	July	715	"			P. S. Commission Reports	
	August	630				"	"
	September	530				"	"
1915	July	732				"	"
	August	896				"	"
	September	Out of Order				"	"
1916	July	838				"	"
	August	810				"	"
	September	785				"	"
1917	July	947				"	"
	August	873				"	"
	September	780				"	"

THE MONTANA POWER COMPANY

Missoula, Montana

MISSOULA WATER DISTRIBUTION
SYSTEM CONSUMPTION

FROM

DAILY SYSTEM REPORTS 1917-1933

MONTHLY AVERAGE					TYPICAL DAY						
Year	Month	Avg. Day		Ave. Day M Inch	Date	Max. Flow		Min. Flow		Day	
		MG	M Inch			MG/24 hr.	M Inch	MG/24 hr.	M Inch	Cons. MB	Cons. M Inch
1917	July	15.3	947	15	16	990	10	618	15.1	934	
	Aug.	14.1	873	14	15	928	5	310	14.6	904	
	Sept.	12.6	780	18	13	804	5	310	12.4	767	
1918	July	13.8	854	25	15	928	11	680	13.7	847	
	Aug.	12.8	792	15	14	866	11	680	13.2	817	
	Sept.	13.1	811	14	13	804	11	680	12.8	792	
1919	July	14.1	873	14	16	990	10	618	14.1	873	
	Aug.	12.0	742	13	16	990	9.5	587	12.4	767	
	Sept.	10.9	675	14	11.2	693	8.5	526	10.9	675	
1920	July	13.8	855	16	15	928	10	618	13.3	823	
	Aug.	13.4	830	16	15	928	11	680	13.9	866	
	Sept.	11.6	718	21	12	742	10	618	11.4	705	
1921	July	14.0	865	14	16	990	11	680	14.7	910	
	Aug.	13.9	860	13	16	990	10	618	14.7	910	
	Sept.	10.7	662	15	11	680	9	557	10.4	644	
1922	July	12.8	792	14	16	990	10	618	11.9	735	
	Aug.	12.1	749	10	15	928	10	618	12.5	774	
	Sept.	11.8	730	15	14	866	10	618	12.2	755	
1923	July	12.7	785	14	16	990	11	680	13.0	805	
	Aug.	13.2	817	14	16	990	11	680	13.7	847	
	Sept.	12.8	792	14	15	928	11	680	13.0	805	
1924	July	10.7	662	11	14	866	6	371	10.7	662	
	Aug.	9.8	606	11	14	866	6	371	10.3	637	
	Sept.	7.6	470	14	12	742	5.5	340	7.9	489	
1925	July	10.9	675	10	15	928	7	433	11.2	693	
	Aug.	10.1	625	9	15	928	7	433	11.3	700	
	Sept.	7.4	458	11	10	618	6	371	7.3	451	
1926	July	12.8	792	13	17	1051	9	557	13.4	829	
	Aug.	10.6	656	16	16	990	7	433	11.3	700	
	Sept.	8.0	495	9	10	618	6.5	402	8.1	500	
1927	July	13.2	817	15	16	990	8	495	13.2	817	
	Aug.	11.1	686	17	15	928	8	495	10.4	643	
	Sept.	8.4	520	13	9	557	7	433	8.0	495	
1928	July	10.1	625	13	15	928	7	433	10.9	675	
	Aug.	10.9	675	14	15	928	6	371	11.7	724	
	Sept.	8.3	514	21	9	557	6	371	7.5	464	
1929	July	13.1	811	15	17	1051	8	495	13.6	841	
	Aug.	12.2	755	14	17	1051	8	495	13.8	854	
	Sept.	9.4	581	24	10	618	6	371	8.0	495	
1930	July	12.8	792	13	16	990	8	495	12.9	798	
	Aug.	11.7	725	15	15	925	8	495	11.5	711	
	Sept.	9.5	587	19	10	618	8	495	9.0	556	
1931	July	12.0	743	17	18	1112	7	433	12.5	774	
	Aug.	10.8	669	19	17	1051	6	371	11.0	680	
	Sept.	7.3	452	15	8	495	5	310	6.8	421	
1932	July	11.4	705	15	16	990	7	433	11.4	705	
	Aug.	10.8	669	15	16	990	7	433	12.0	742	
	Sept.	8.6	532	16	14	866	6	371	10.3	637	
1933	July	12.3	761	14	16	990	8	495	12.9	798	
	Aug.	9.7	600	13	17	1051	6	371	11.0	680	
	Sept.	6.6	408	16	7	433	5	310	6.7	415	
1933	Jan.	Avg.		375							

(Testimony of H. S. Thane.)

During my knowledge and recollection of Rattlesnake creek, I know of no addition to the natural flow of that stream from any source to that part of the stream below the "dam" as now located and shown on the map. I have heard reference to water that may be observed at times in the bed of Rattlesnake creek at a point close to the Hollenbeck ditch intake and have observed water at that point at times. The source of that water in my opinion is creek water that has flowed over the "dam" and has arisen at that point, if it went down. Sometimes it flows continuously. I have observed the presence of water in the bed of the stream at about the location of the head of the old Mill ditch, and at times when there was less water above.

Q. And from your experience and observation, to what source do you attribute that water?

The COURT: What water is this, now?

Mr. WILSON: We object to that upon the ground that it would be immaterial what the source of it is if it is Rattlesnake Creek water unless it comes from an independent source there outside of the watershed of the Rattlesnake.

The COURT: You may answer. Insofar as not entitled to consideration the Court will give it none.

Mr. WILSON: Exception.

A. I think it is water that came down the stream at some prior time.

The COURT: I guess you all agree on that.

Mr. WHITLOCK: I don't know.

(Testimony of H. S. Thane.)

In my opinion, the water being observed at the head of the Mill ditch when there is no water at points above may be [178] accounted for from the fact that the flow over the "dam" in dry seasons is intermittent; it takes time for the water which passes the "dam" to reach the head of the Mill ditch, so that it is possible that if you observe it at certain times you will find none up above and some water below. The time required in days or hours for the water to get down to the head of the Mill ditch is quite variable, and I could not make a general answer to that. If the flow is large and the stream full of water it is only a matter of hours, and if the stream is dry, it would be a matter of days or weeks. As to whether or not a larger or smaller amount should be observed in the morning at the head of the Mill ditch rather than at other times of the day, there would be a larger amount in the morning as there has been an intermittent flow over the "dam", which was at its maximum in the early hours. If most of the water ran over the dam at, say, 2:00 o'clock in the morning and decreased or stopped I think that the reflection on Pine Street at the head of the Mill ditch would show more water in the morning than it would in the afternoon. I have made observations at the head of the Mill ditch and observed and read the weir in 1926, testified to by Mr. Tucker. The weir was completed on July 15th or 16th—a 10-foot weir. At 11:50 of July 16th the depth of water over the weir was four and three

(Testimony of H. S. Thane.)

quarters inches, equivalent to 340 miners inches; again at 11:40 and 11:50 on July 16th and 17th there was 340 miners inches; on the 26th at 1:40 P. M. there was 210 miners inches; on the 30th at 11:40 A. M., 139.2 miners inches and on August 3rd at noon, 148.4 miners inches; on August 10th, the weir had been removed. The amounts of water according to my records, were constantly diminishing. I explained the presence of water [179] at the head of the Mill ditch by the fact that if the water is shut off at the "dam" so that the creek bed is dry, the water will appear at the head of the Mill ditch for some time. It will gradually decrease and may be some water there for weeks. I don't know how long it would take to stop running, but it is my opinion that it would ultimately stop running if there were none coming in over the "dam".

I made some other measurements at the head of the Mill ditch in the year 1929, and these are the results:

A. On September 20th, 1929, I measured the creek at Pine Street, (head of Mill ditch) at 3:30 p. m. with a current meter and found a flow of 121 miners inches. Then we installed a weir there which was completed on October 23rd, 1929. At that time there was 52 miners inches at 3:00 p. m. And on October 24th, at 11:00 a. m. there was 47 miners inches. On October 25th at 4:40 p. m. there was 38 miners inches. And those readings continued about that way until November 2nd, when we had 62

(Testimony of H. S. Thane.)

inches. It had increased slightly. And I continued the readings until November 16th, when it showed 101 inches. These quantities—I estimated five miners inches leakage, so I think that should probably be increased five inches. That would make the minimum reading 43 inches, and the minimum reading was what I was interested in primarily.

Q. Mr. Thane, if you were dealing with a volume of water which we will fix at 946 inches, having in mind two points for diverting it, one being the head of the old Mill ditch and the other being the present dam of the defendant company located as you have indicated, at which point of diversion would there be the smaller amount of water left in the stream for use of those users located between the dam and the head of the Mill ditch? [180]

Mr. WILSON: That is objected to upon the ground that it is not a subject upon which the witness may express an opinion, and passing upon the result which the Court must determine.

The COURT: I think sustained.

Mr. WHITLOCK: This witness is an expert, if your Honor please—

The COURT: That is the very issue. Proceed.

At the “dam” the flow of water is regulated by automatic volume valves. As there is more demand for water in town, the pipe automatically lets more water in. When the demand decreases, the pipe automatically reduces, and water not used through

(Testimony of H. S. Thane.)

that automatic control goes over the "dam" down stream.

Q. Have you any figures here, Mr. Thane, as to the cost of the diversion works of the defendant company?

Mr. WILSON: To which we object upon the ground that it is not material in this case, if your Honor please; upon the ground that the defendant's rights cannot be—to the use of water could not be increased by the construction of their diversion works.

Mr. WHITLOCK: It bears on the question of laches.

The COURT: Well, it may be immaterial, but it is in their answer, and if not material and entitled to consideration the Court will give it none. For the sake of the record, overruled.

The original work at the diversion dam was about \$20,000.00; additions in 1924 about \$56,000.00; the pipe line cost about \$85,000.00; the reservoir on the hill about \$22,000.00; [181] and the distribution system represents in excess of \$500,000.00. Since 1902, there has been expended in repair and in replacement in the system upwards of \$150,000.00, of which \$56,000.00 was in diversion works in 1924, when we replaced the existing wooden dam with a reinforced concrete structure on the same foundation. When the defendant acquired the system, its book value was \$1,000,000.00 and since then \$25,000.00 has been expended in repairs, also an additional one-half mile of pipeline replacement, costing \$15,000.00.

(Testimony of H. S. Thane.)

From the records it appears we were using just about as much water in 1905 as we are now using in 1933. In between, the use fluctuated, but not greatly; the table shows, and I believe, there has not been any material change in the amount of water used in the last 15 or 20 years.

CROSS EXAMINATION by Mr. Mulroney:

The water-works designated on the map, defendant's Exhibit 6, was before my time and I can't testify to that except the information I received. Exhibit 8 states the average number of inches used per day in each month listed from 1905 to the present time, for instance the very first one, November 1905, 309, that would be the average inches used per day during that month, and so on all the way through. Adding right No. 1, 946 inches and right No. 2, 160 inches makes 1106 inches; and if you add what defendant had for right No. 3, being $13\frac{1}{2}$, No. 4 being 65, No. 8 being $46\frac{1}{2}$, No. 9 being 348 and No. 14 being 645, I have 1118 inches, in addition to 1106 for rights No. 1 and 2 and the other rights acquired by defendant amounting to 502 inches, making a total of 2726 inches, which is the total amount claimed by the defendant. [182]

Referring again to Exhibit 8, it appears that the amount used in November, 1905, which was 309 inches, gradually increased to a top of about 896 inches. November is not in the irrigation season,

(Testimony of H. S. Thane.)

and more city water is used in irrigating season. If we had the records for the 1905 irrigation season, I expect it would be comparable and not greatly different in amounts from the rest of the irrigation seasons. For instance July and August of 1910 being 495 and 565 respectively, and the amount has increased so that in 1917 in irrigating season it reached 900 inches or thereabouts. The average consumption for 1913 is 767 inches for August, 408 inches for September and the highest amount, maximum rate of flow, shown in Exhibit 8 is 1112 inches, and that is the flow for July 1931, which is the highest that is shown, I think, on Exhibit 8 and is higher than the average. Excluding the Higgins and Mill ditches, defendant would still have 770 inches, which is about the average amount used from 1905 to 1910, but is not higher than the peak. The pipe of defendant from the dam to its reservoir, calculating roughly, is 1500 miners inches, which is probably what it would carry if pushed to the limit; while defendant claims to own 2726 inches, which includes the agricultural rights, I don't think defendant ever carried quite 1500 inches through its pipe.

I have never seen Rattlesnake creek dry at the head of the Mill ditch, almost but not quite. There is seldom 24 hours that water doesn't go over the dam at all. I haven't been at the head of the Hollenbeck ditch to know whether or not there are times when water does not flow past that point.

(Testimony of H. S. Thane.)

REDIRECT EXAMINATION by Mr. Whitlock:

[183]

There are two channels of the creek near the head of the Hollenbeck ditch; they are shown on the map. The channel forks at a point below the "dam" and come together again further down.

Mr. WHITLOCK: If the Court please, while this witness is on the stand, to preserve the record, I desire to make an offer of proof along the line suggested. I have written it out.

(The defendant's Offer of Proof No. 1 was submitted to counsel for the plaintiffs.)

Mr. WILSON: We object to the offer on the same grounds stated in the objection to the question upon the same point.

The COURT: Well, read it.

Mr. WHITLOCK: "We offer to prove by the witness now on the stand that it is his opinion from observation of Rattlesnake Creek that if the water now diverted by the defendant at its dam were allowed to flow down to the head of the Mill ditch and were there taken out that there would be a loss in the quantity in the stream and that there would therefore be less available for supply of agricultural rights of the plaintiffs."

Mr. WILSON: Our objection is that it is not a matter upon which——

The COURT: That is obvious. Whatever water goes over the dam there is necessarily some evaporation, whether there will be seepage or not to take its place. Objection sustained. [184]

Mr. WHITLOCK: Exception.

JOHN M. BRECHBILL,

called as a witness on behalf of the defendant, and being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Whitlock:

My name is John M. Brechbill. I have been a carpenter all my life, but I am running an elevator now. I was in the contracting business once, and have lived in Missoula about 37 or 38 years. I know the location of defendant's diversion dam on Rattlesnake. I built the dam in 1902, starting in the fore part of June after the freshet went down in 1902 and finishing so that water was running through right after the first of December of the same year, and water was diverted to supply Missoula before the end of the year, I am certain; and the city supply has never been changed since then.

The dam was built on 12 by 12 fir timber on bed rock, a permanent structure, with concrete foundation, extending clear across the creek. We did blasting in the construction. The dam lasted until it was torn out in 1923, and a concrete dam was built right on the same bed rock and location. The new dam was a little wider at the bottom than the old one.

Mr. WHITLOCK: We have an admission that counsel have agreed to to shorten the record, your Honor. The defendant herein is the successor in interest by mesne conveyances of the Missoula Water Company, the plaintiff in cause No. 1953 heretofore tried in the District Court of the Fourth Judicial District of the State of Mont- [185] ana in and for the County of Missoula, and its predecessors, and

(Testimony of John M. Brechbill.)

has succeeded to all of the property of said company and its predecessors, including the water rights decreed to it in said cause. The defendant is and its predecessors in interest were at all the times referred to in the pleadings herein public utilities, owning and operating the water system and works used to divert water from Rattlesnake Creek, the stream involved in this action, and distribute said water to the city of Missoula, Montana, and its inhabitants, and fire protection and general household, domestic, irrigation and other useful purposes, this defendant and its predecessors being authorized to engage in the sale and distribution of water, and being the owner of the franchise granted by the City of Missoula, a municipal corporation, of the State of Montana, giving a perpetual right to the use of the streets and alleys of said city for pipes used to serve the city and its people.

Mr. WILSON: Well, I think we can agree to that with this qualification, that we do not agree that the fact of its being a public service corporation increases its rights.

The COURT: Certainly.

Mr. WILSON: But it has succeeded to such rights as its predecessors had.

T. T. McLEOD, [186]

called as a witness on behalf of the defendant, being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Whitlock:

My name is T. T. McLeod; I live at Mill City, Oregon. I formerly resided in Missoula and left

here in 1911. Up to that time I was familiar with the water works system supplying Missoula. My acquaintance with the system began in 1893. I was manager of the water works during that period, and Missoula Water Works and Milling Company owned the system. I ceased being manager in January, 1907. I have been up to the dam where the water is now being diverted to the system, in the last few days, and recognized the location of the dam upon the maps in evidence here. In 1893, the water was being diverted to furnish the city of Missoula at a point on Rattlesnake, between a quarter and a half mile below the Fedderson ranch and barns, which point is shown on defendant's Exhibit 6 by the words "water works". My memory is refreshed as to this by my recent visit, and my answer is given in the light of my recent visit. The point of diversion for the city supply was changed and the new pipe line built in 1902 from the point shown on defendant's Exhibit 6 with the words "water works" to the present point of diversion at which the present dam is located, and I have verified that by my recent visit. The work for the diversion at the present location commenced in 1902 and was finished the same year; and from then forward the water for the city supply was diverted at the present diversion dam, and the point of diversion previously used was abandoned.

Q. What was the reason for going up to the present point?

Mr. WILSON: That is objected to upon the

(Testimony of T. T. McLeod.)

ground that [187] it is immaterial and has no bearing upon the issues in this case.

The COURT: Oh, I should think so. Get more fall?

Mr. WHITLOCK: That was one of the reasons, your Honor.

The COURT: He may answer. For the sake of the record. Overruled.

Mr. WILSON: Exception.

The water was contaminated and we wanted to get higher up on the stream, so as to get a greater head. I remember the old ditch, called here Mill ditch, and it was used in the old days for running the flour mill, but that was before my day in Missoula. I knew the old Higgins ditch. It came out of Rattlesnake just below the water company's old diversion point that we abandoned, and ran down to what we knew then as the Marshall ranch west of town. Water that was flowing in either the Mill ditch or old Higgins ditch, if wasted out of the ditches, or when used from those ditches, would not find its way back into Rattlesnake Creek. Those ditches were being used when I came to Missoula in 1893.

Q. Now, in your capacity as manager of the company, which you say began in 1893, what water rights were you claiming through the old flume?

Mr. WILSON: That is objected to, if your Honor please, upon the ground that the water rights of the predecessors of the defendant were fixed and

(Testimony of T. T. McLeod.)

determined by the decree in cause No. 1953, and the defendant may not now vary, contradict or impeach that decree.

Mr. WHITLOCK: No intention of doing that. Merely that at the time when the point of diversion was [188] changed to this present point this decree was rendered.

The COURT: Well, he said so. The point of diversion was changed in 1902.

Mr. WHITLOCK: But I am asking him as to the rights they claimed to use before the old point of diversion——

The COURT: Well, are you claiming any other rights than this decree gives you?

Mr. WHITLOCK: Certainly not, your Honor, but we are trying to ascertain what rights were claimed to be used through the old water works ditch.

The COURT: Before the decree?

Mr. WHITLOCK: Before the decree. The decree is silent.

The COURT: I think you may answer. Overruled.

Mr. WILSON: Exception.

A. We used the water that the company claimed as their oldest rights. That is my understanding of that.

Q. The company at that time was the owner of the old Mill right, was it not?

A. Yes sir, yes.

(Testimony of T. T. McLeod.)

Q. And the use or the place of use through which you claimed those old rights was the one that you have located——

A. Yes.

Q. —— on the map, that is marked “water works?”

A. Yes, yes sir.

Q. And when you moved up from that point to the present location of the dam, did you continue to use those rights and claim them?

A. No, the lower—— [189]

Q. You abandoned the old ditch?

A. That is it. We used it up to then.

Q. What about the rights? Did you claim the same rights?

A. We claimed the same rights.

Q. Did you have any intention of giving up your water rights?

A. None. I never heard of such a thing.

The Mill ditch and the old Higgins ditch were discontinued, both ditches in 1906; and while I was here and at the time the property was purchased by Senator Clark. Before that time and before the two ditches were finally discontinued, the amount of water flowing in them kept diminishing. After we moved up to the new point in 1902, the water was diverted through a closed pipe; formerly at the old point, we used just a common flume; we just had a wing dam in the creek bed and a wooden flume led out, and the water came into the flume, which was covered over with plank and dirt. The

(Testimony of T. T. McLeod.)

pipe line is more efficient, and when the pipeline was installed, we used less water, which continued until I left in 1907. There was no source of supply during the time I was connected with the water company bringing additional water into Rattlesnake between the point of location of the present dam and the head of the old Mill ditch.

I didn't do much to keep up the Higgins and Mill ditches while I was in charge here, kept them open a little so that we could get water through them—the Mill ditch; we cleaned them out a little; we couldn't get enough to supply Mr. Newton that year. We did no work of upkeep on it or on the Higgins ditch.

CROSS EXAMINATION by Mr. Mulroney:

From 1893 up until the time of the change in 1902, the point of diversion of the water company was above both Mill ditch and the old Higgins ditch. During the years 1902, 1903 and 1904, I would say we used more than 300 or 400 inches of water, but I couldn't tell you how much more. I have only one [190] measurement of it in the ditch. I have a record of a measurement in April on the old flume; I can't remember the year; and we were using about 9,000,000 gallons. The engineer will have to figure how many inches that is, for I don't know. I think we used more than 300 or 400 inches prior to 1905. It would not be much different in 1904, 1905, and 1906 than it was in 1901, 1902 and 1903. The company claimed to use the rights that were the earliest rights. I was present at the time the

(Testimony of T. T. McLeod.)

decree on Rattlesnake was entered in 1903, and we used the water; and it was my understanding that we were entitled to the oldest decree. It is true that we made no claim to this right, that right, or the other right, but merely turned water into the head of the works and let it run. It was under the decree. My memory is that the Higgins ditch and the Mill ditch were closed in 1906, and that they were operated up until 1906.

C. H. McLEOD,

called as a witness on behalf of the defendant, being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Whitlock:

My name is C. H. McLeod; I have lived in Missoula 53 years. I was a director of the Missoula Water Works and Milling Company that owned the water works in the 90s. The principal use made of that water by the company was for irrigation, water power, and city use. In the latter 90s, the water was diverted out of Rattlesnake near the Fedderson ranch.

Q. What rights did your company claim at that time?

Mr. WILSON: To which we object upon the ground, if your Honor please, that the rights to the use of the waters of Rattlesnake Creek were set-[191] tled and adjudicated in the decree in cause

(Testimony of C. H. McLeod.)

No. 1953, which is conclusive upon all parties and their successors, and may not be contradicted or——

The COURT: Any new parties in this action? Are there any new parties in this action?

Mr. WILSON: I don't think so. There are none so far as I know. These are all parties or successors to parties in cause 1953, both plaintiffs and defendant in this action.

Mr. WHITLOCK: Plaintiffs claim to be successors in interest to those who were parties to that action.

The COURT: I think he may answer, and if it is not material or competent or entitled to consideration the Court will give it none. For the sake of the record, overruled.

Mr. WILSON: Exception.

(The question was read by the reporter.)

A. Well, we claimed, I think, 160 inches in the Higgins ditch.

Q. How about the Mill ditch?

A. Well, we claimed—I don't remember but it was all the ditch would carry; whatever it would carry we claimed the Mill right, yes sir.

Q. Did you claim to use those rights for furnishing Missoula?

Mr. WILSON: That is objected to upon the ground that it is hearsay and not any fact upon which water rights could be based.

The COURT: Well, I don't know how you are going to identify the rights except by what they intended or what they were doing. Overruled. [192] You may answer.

(Testimony of C. H. McLeod.)

Mr. WILSON: Exception.

The COURT: If it is not entitled to consideration the Court will give it none.

Q. Did you claim to use the Mill right and the Higgins right to furnish the city of Missoula?

A. Yes sir.

Q. From the point that you have referred to?

A. Yes sir.

Q. And do you know whether or not the point from which you furnished Missoula was thereafter changed?

A. It was.

The point of diversion was moved up stream to the present location of the water works dam. I have observed Rattlesnake Creek and its water condition at the head of old Mill ditch. During the years that I have lived here I have had occasion to observe Rattlesnake Creek frequently and with particular reference to that part of the stream where the old Mill ditch used to take out. I have seen some seasons that there was no water in that stream at that point. I can't tell just how many seasons but I expect ten or fifteen years since I have been here when the stream was dry at that point.

CROSS EXAMINATION by Mr. Mulroney.

You understand me to say that at the point where the old Mill ditch came out down by the Northern Pacific trestle—

In the course of my observation here I have seen

(Testimony of C. H. McLeod.)

it absolutely dry some ten or fifteen times. During all the years that I have been here I think that the Mill ditch had water in it every year up until 1906 and that is also true of the Higgins ditch. I think perhaps the water was curtailed in those ditches some years when there were very dry years in order to give the city a proper supply.

REDIRECT EXAMINATION by Mr. Whitlock.

Q. The city use was the principal use, as I understand it.

A. Yes, sir, that came first.

WALTER M. HAY,

called as a witness on behalf of the defendant, being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Whitlock:

I have previously testified for the plaintiffs and I knew the old Higgins ditch. It ran through town here in the four hundred block on Spruce Street, then it crossed to this [193] (the south) side of Spruce. I can't tell the exact location as to say whether it crossed Higgins Avenue. My best judgment is the Mill ditch was discontinued in the fall of 1905 and the Higgins ditch was discontinued two years before that, which would be about 1903 or 1904.

(Testimony of Walter M. Hay.)

CROSS EXAMINATION by Mr. Mulroney:

I am not positive whether Mill ditch was closed in the fall of 1905 or the spring of 1906, but the Higgins ditch was closed two years before that, as I remember; but I am not positive of the dates.

REDIRECT EXAMINATION by Mr. Whitlock:

I lived in the 400 block along the Higgins ditch; it ran along the side of the street, and I was over to it.

C. H. CHRISTENSEN,

called as a witness on behalf of the defendant, being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Whitlock:

My name is C. H. Christensen; my business is manager of the Missoula division of the Montana Power Company, the defendant in this action, and I held a similar position with its predecessors, the Missoula Public Service Company and the Missoula Light & Water Company. I have been connected with the water utility supplying Missoula since 1893. Defendant acquired the system November 1, 1929. I know the location of the dam where water is diverted to furnish Missoula and its inhabitants, and have known that location since 1902; water has been diverted at that point since then continuously and no other point of diversion has been used since that date by the companies owning the utility. The change made in 1924, was to rebuild the dam, which

(Testimony of C. H. Christensen.)

was formerly timber and which is now concrete. The point [194] of diversion was not changed. I remember where water was diverted prior to 1902 to supply Missoula, which was about an eighth of a mile below the Fedderson barn and above the old Higgins ditch, and of course, the old Mill ditch, which two old ditches I remember; and I also remember the old water works flume. I don't remember the year when the use of the Mill ditch was discontinued, but I know it was discontinued. The water suit to determine Rattlesnake Creek rights was tried in 1902 and decree thereafter signed. The water was being diverted at the present point in 1902.

Q. Now, since your connection with the company, Mr. Christensen, what rights have you claimed to use from Rattlesnake in furnishing the city of Missoula and its people with water?

Mr. WILSON: We object to that as calling for hearsay, a self-serving declaration and immaterial, and not testimony of any fact involved in the issues in this case.

Mr. WHITLOCK: I am asking in his capacity as manager of this company.

The COURT: I think you may answer, and if not competent or material the Court will ignore it in making up its decision. Objection overruled.

Mr. WILSON: Exception.

A. We did not use any particular right. We used out of your first three rights, 1118½ inches, all the water that was demanded by the system.

(Testimony of C. H. Christensen.)

When I say our first three rights, I included the Mill right, the original Higgins and a 13½ inch right. I knew the conditions of Rattlesnake Valley as to irrigation prior to 1902. As a young man, I worked in the Rattlesnake Valley, in 1893, and [195] there was very little land under cultivation in that section where the poor farm is now or where the poor farm then was. I have observed the water supply available for agricultural use, both before and after the year 1902.

Q. What have you to say as to whether or not there was more or less available after 1902?

A. There was less—there was more.

Mr. WILSON: That is objected to because it is all concluded by the decree in cause No. 1953, which cannot be impeached or contradicted by any party.

The COURT: What is the object?

Mr. WHITLOCK: I am trying to show now from this witness, if he knows, the extent of the use of this particular defendant and its predecessors, and the effect that it may have had, having in mind the amount of water it used and the amount left for other use.

The COURT: Well, I can't see that it is very material. We will let him answer and have it in the record, and insofar as it is not material or competent the Court will ignore it in making up its decision. Overruled.

Mr. WILSON: Exception.

There was more water available after 1902, which

(Testimony of C. H. Christensen.)

was after we moved up to the present point. The works, particularly the dam, by which the water is diverted and furnished to Missoula, is a dam 13 feet high and 50 or 60 feet wide, and an earth dam that is a couple of hundred feet long and extends up through the mill pond over to the eastern shore of the creek. The dam, of course, can be easily observed in the stream. The water is [196] conveyed from that point by a pipe to a circular distributing reservoir that defendant has just north-east of town, which is 17 ft. deep, 105 feet in diameter and contains 1,000,000 gallons of water. It is concrete, and was built also in 1902, and put in use that year; it has been used continuously since that year. During my managership, I have claimed the right to use these structures for the diversion of water for defendant, and such use has not been interrupted nor interfered with.

CROSS EXAMINATION by Mr. Mulroney:

I have been an employee of the company since 1893, and have been familiar with the stream during that period. I think 1600 or 1700 inches is a high estimate of the flow during July and August, but that must be so if the water commissioner's reports so show. From my own observation, I would say 1400 inches. The chart, Exhibit 8, shows my company used 300 or 400 inches in 1905, which is about right. I have no recollection as to that time. All I know is from the chart. From my recollection and experience, I would say that the use in 1905 was about as it was in 1902, 1903 and 1904, and also prior to that time, so that when the change

(Testimony of C. H. Christensen.)

was made from the water works flume up to the dam in 1902, we were using presumably 300 or 400 inches of water, which continued to about 1905, when it increased, and I think we now average about 900 inches, and that is in July and August, when people have to irrigate.

As to the claim to specific water rights used in 1902, I had nothing to do with that then, and I don't know what claim was made at all in 1902 nor until 1914. I was an employee of the water company in 1902 and the change was made as indicated in that year. I can't say as to the amount of water used; I don't know how much was used through the flume before the change was [197] made in 1902. The reason that I answer that there was more water for the farmers after the water company's point of diversion was moved up, is because I used to go fishing in Rattlesnake Creek before 1902 and there was always plenty of water and good fishing, and there wasn't anything after 1903 and 1904; after the Mill ditch and Higgins ditch were abandoned there wasn't any more water—much more water in the creek than there is now in the summer time.

Q. Well, of course, those ditches carried water, you say, up to about 1906?

A. Well, whatever year it was.

The COURT: Well now, let's get this straight. You say you judged after 1902 there was more water available for the farmers?

(Testimony of C. H. Christensen.)

A. Up above.

The COURT: Above?

A. Above the dam.

The COURT: Above the dam?

A. Yes sir.

The COURT: What ditches are taken out above the dam?

A. Well, those three ditches were taken out above the dam.

The COURT: But after the dam was put in there was less water below?

A. There was very little water down below.

The COURT: After you put in your dam?

A. Yes sir.

REDIRECT EXAMINATION by Mr. Whitlock:

There were many ditches down below used by agricultural users after the dam was put in. After the change to the dam was the time when the district up there began to build up [198] around the poor farm. Going back to the time before the Higgins and Mill ditches were discontinued, the farmers had less water than they had after the Higgins ditch and Mill ditch water was diverted at the reservoir.

RECROSS EXAMINATION by Mr. Mulroney:

I know that the only ditches taking out above the dam are the Effinger, 100 inches, the Williams, 160 inches, the Quast, 328 inches and Kemp 100 inches, and if the water company only took 300 or 400 inches, that wouldn't take the whole flow of the

(Testimony of C. H. Christensen.)

creek up there, but the demand is greater at times during the day than at other times, and we may have required more than 400 inches; it would depend on what the maximum demand was. The reservoir is full all the time, and the flow into the pipeline may be as high as 1100 inches during the day time or as low as 300 inches during the night time. From 1902 to 1924, the pipeline would carry about 24,000,000 gallons, 1450 to 1500 inches, and that was its carrying capacity before and since 1924, although it has never carried that much.

The COURT: How much water does the city use a day? You said something about 24,000,000 gallons.

A. It has been as high as 18,000,000 gallons during the 24 hours, and at the present time it is five and a half millions.

The COURT: Where do you use the rest?

A. Sir

The COURT: Well, any discharge or waste from your reservoir? How do you regulate it?

A. That regulates itself. There is a volume valve and that opens and closes as the reservoir level lowers or rises.

The COURT: All right. Anything further?

[199]

Mr. WHITLOCK: We desire at this time to offer in evidence a certified copy of the amended complaint in cause No. 1953, being the water adjudication case.

Mr. WILSON: We have no objection.

DEFENDANT'S EXHIBIT 9,

the certified copy of amended complaint above mentioned, so admitted in evidence without objection, is in words and figures as follows, to-wit:

IN THE FOURTH JUDICIAL DISTRICT
COURT.

State of Montana,
County of Missoula.

The Missoula Water Company, a Corporation,
Plaintiff,

vs.

Charles E. Williams, Missoula County, John E. Johnson, Elmer E. Hughes, John White, Harry Mattison, Ollie D. Mattison, B. F. Nesmith, Mary F. Nesmith, Andrew Schilling, Mamie E. Murray, Charles Owens, Harvey Biggs, Henry C. Hollenbeck, Thomas P. Street, William Mattison, R. M. Cobban, John Smith, W. H. Raymond, Wallace P. Smith, J. B. Frazier, E. R. Kilburn, J. W. Connelly, Sebastian Effinger, George A. Duncan, James S. Kemp, Otto Quast, Jacob G. Ambrose, John Adams, E. J. Waitman, W. F. K. Beeskove, Arthur Franklin, F. L. Pelcher, G. E. Van Buren, Missoula Real Estate Association, Peter Federson, W. R. Hamilton, H. E. Day, John Harkness, Theodore LaChambre, A. B. Hammond, Cluff. Vasser, William Neil, John Capp, Mrs. E. J. Clements, C. H. Moss, Joel A. Moss, John Barrett, A. A. Settlemire and Rufus Striker,
Defendants. [200]

Now comes the above named plaintiff, leave of Court having been granted to file its amended complaint, and complains of the above named defendants, and for cause of action, alleges:

I.

That the plaintiff is a corporation duly organized and existing under and by virtue of the laws of the State of Oregon, and as such corporation is now doing business in the State of Montana, having filed in the office of the Secretary of the State of Montana, and in the office of the County Clerk of Missoula County, this State, all of the certificates and statements, and having done all things required by Section 1030 of the Civil Code of Montana, to authorize a foreign corporation to do business in this State.

II.

That the purposes for which said corporation was organized, were, among others, the right to acquire, equip, own, maintain, and operate water-works, reservoirs, ditches, flumes, dams, pipes and other facilities for storing, having and disbursing water, for irrigating, power and domestic purposes within the State of Montana; to purchase, or otherwise acquire and appropriate the waters of any stream, lake or water supply, and to conduct the same for sale and distribution.

III.

That the plaintiff under the powers contained in its articles of incorporation has purchased and

become the owner of valuable water rights, and the owner of the use of a large quantity of water appropriated and diverted from Rattlesnake Creek in the County of Missoula, this State, for the purpose of supplying the inhabitants of the City of Missoula and vicinity with pure, fresh water for domestic, agricultural, mechanical and other useful and beneficial purposes, among which are, to protect and secure the lives and safety of the property of the inhabitants of the City of Missoula, and vicinity from fire and conflagrations, all of which are public uses.

IV.

That the defendant, Missoula County, is a municipal corporation organized by the laws of the State of California.

V.

That the defendant, Missoula Real Estate Association, is a corporation duly organized and existing under and by virtue of the laws of the State of Montana.

VI.

That the plaintiff is now and for a long time prior hereto, has been the owner of a franchise granted to its predecessors in interest by the Common Council of the City of Missoula, this State, said City being a municipal corporation duly organized and existing under and by virtue of the laws of Montana; and that under and by virtue of such franchise the plaintiff and its predecessors in interest, have at a heavy expense and by the

expenditures of large sums of money, laid and constructed water mains and pipes throughout the principal portions of the City of Missoula, and for more than twenty-five years last past have conveyed through said water mains and pipes water appropriated and diverted from the said Rattlesnake Creek, as aforesaid, and have during all of said time supplied the City of Missoula and the inhabitants thereof, and vicinity, with water for the public uses, as aforesaid, and that the plaintiff is now supplying the inhabitants of the said City of Missoula and vicinity with water for the aforesaid purposes and intends to continue so to do. [202]

VII.

That the plaintiff in and during the year 1864 by and through its grantors and predecessors in interest, by means of dams, ditches and flumes diverted, appropriated and used the waters of Rattlesnake Creek to the amount of Two thousand (2000) inches, and afterwards, by and through its predecessors in interest, to-wit, in the year 1868, by means of dams, ditches, head-gates and flumes did divert, appropriate and use of the waters of said Rattlesnake Creek to the amount of twelve hundred (1200) inches, and did, by and through its predecessors in interest, by means of dams, ditches and flumes, divert and appropriate of the waters of said creek in the year 1868 one thousand (1000) inches; that said water and the whole thereof was diverted and appropriated from the said Rattlesnake Creek in the County of Missoula, State of

Montana, for mechanical, agricultural, domestic and other useful and beneficial purposes; that said diversion and appropriation made by the plaintiff of the waters of said creek amount in the aggregate to forty-two hundred (4200) inches, measured according to the laws of the State of Montana for the measurement of water; that from the time of the first appropriation of said water in 1864 up to the present time, the said plaintiff and its predecessors in interest have continually used the waters of said creek, and so much thereof as have from time to time been necessary during said time for the purpose for which the same was appropriated, except at such times when the plaintiff or its predecessors in interest were deprived of the use of a portion of said water by the acts of the defendants, or some one or more of the said defendants herein, and that the said water and the whole thereof is, was and will be [203] necessary and required by the said plaintiff for the purpose for which the same was appropriated as hereinabove alleged.

Plaintiff further alleges that it has a contract with the City of Missoula, made with the Common Council thereof, and duly signed by the proper authorities of said City, by the terms of which the plaintiff is required to furnish said City with a sufficient quantity of water for all of the public uses required by the City, principal amongst which is to furnish water to extinguish fires and prevent conflagrations in said City; and under its franchises aforesaid, is required to furnish water to all of the

inhabitants of said City, for domestic and other useful and beneficial purposes whenever required so to do by them, or any of them, and is now, and for many years last past been doing so.

IX.

Plaintiff further alleges that the defendants, and each and every one of them, claim to have made appropriations of water from said Rattlesnake Creek, and claim the right to divert and use said water from said creek, and for a long time past have been, and now are diverting and using water from said creek to which the plaintiff is entitled by virtue and reason of plaintiff's prior right to the same, acquired by prior appropriation thereof, made by the plaintiff's grantors and predecessors in interest as aforesaid.

X.

That all of the appropriations of water claimed to have been made from the said Rattlesnake Creek by the defendants, or any of them, and all and each of their rights to the use thereof, were made and acquired, if at all, subsequently to the time that the plaintiff acquired the right to the use of [204] said water by and through the appropriation thereof made by plaintiff's grantors and predecessors in interest, as aforesaid alleged, of all of which the plaintiff is now the owner.

XI.

That for more than two years last past, the defendants or some of them, have, during the sum-

mer and fall of each year, when the water was low and scarce in said creek, continually diverted large quantities of water from said creek, to the use of which the plaintiff was entitled by reason of the prior appropriation made by the plaintiff's grantors and predecessors in interest as aforesaid, thereby depriving the plaintiff of the use thereof, to its great damage and detriment.

XII.

That the defendants have been requested by the plaintiff, by and through its manager, to cease diverting said water and depriving the plaintiff of the use thereof, and they have often agreed so to do, but disregarding the requests and demands of the plaintiff's manager to cease diverting and molesting the waters of said creek, and depriving the plaintiff of the use thereof, the defendants continue to divert said water from said stream, and continue to deprive the plaintiff of the use thereof, and from the acts of the defendants in disregarding the requests and demands of the plaintiff made as aforesaid, to cease diverting and using said water, and depriving the plaintiff of the use thereof, the plaintiff has reason to believe, and does believe, and therefore alleges the same to be a fact, that the defendants intend to, and by their acts as aforesaid, threaten to continue to divert and use said water, to the use of which the plaintiff has a prior right, and deprive the plaintiff of the necessary use thereof, [205] to his great damage and irreparable injury.

XIII.

The plaintiff further alleges that the defendants, Charles E. Williams, John Barett, John Capp, Mrs. E. J. Clements, Otto Quast, William Neil, Jacob G. Ambrose and A. A. Settlemire are now wrongfully and unlawfully diverting and using about one thousand (1000) inches of the water of said Rattlesnake Creek, to the use of which the plaintiff is now entitled by reason of prior appropriation as hereinbefore alleged, and unless enjoined and restrained by the Court, will continue to divert and use said water and deprive the plaintiff of the use thereof.

That the plaintiff by its manager and duly authorized agent has repeatedly requested and demanded of the defendants last above named, to cease using and diverting said water and the said defendants have repeatedly promised so to do, but have failed and neglected to do so, and still continue to divert and use said water to the great damage and injury of the plaintiff. That the manager and agent of plaintiff has on several occasions turned the water away from the ditches of the last named defendants, and turned it into the ditches of the plaintiff, and the defendants last above named have as repeatedly turned it into their ditches again, and deprived the plaintiff of the use thereof.

Plaintiff alleges that notwithstanding the fact that the said last named defendants have promised the plaintiff that they would refrain from using and diverting said water, and depriving the plaintiff of the use thereof, they still continue to divert and use it, and deprive the plaintiff of the use thereof;

and plaintiff alleges, that it has reason to believe and does believe, that the defendants last above named [206] intend to continue to use and divert said water, and that by their acts aforesaid, threaten, and unless restrained by and order of this Court will continue to use and divert said water, and deprive the plaintiff of the necessary use thereof, to its great damage and irreparable injury.

XIV.

That at the present time, and for one month last past, there is, and has been a very low stage of water in said Rattlesnake Creek, and at the present time the plaintiff has not the necessary quantity of water in its mains and water pipe to meet the necessary demands made upon plaintiff for water by the City of Missoula, and the inhabitants thereof, and the reason that the plaintiff does not now have a sufficient quantity of water to supply the demands aforesaid is, that the defendants last herein named, are now diverting and using said water to which the plaintiff is entitled, as aforesaid; that if said defendants last named, were not diverting and using said water to the use of which the plaintiff is entitled, the plaintiff would have sufficient to meet its immediate demands and wants.

XV.

Plaintiff further alleges that owing to the long dry period of weather there is much apprehended

danger of fires occurring in the City of Missoula, and that should a fire occur in said City at the present time, while the buildings are in their present dry and inflammable condition, it would require all of the water that plaintiff's mains and water pipes would carry to successfully fight said fire and to prevent its spreading and destroying much property, and that the supply of water that plaintiff is now able to obtain would be wholly in- [207] sufficient to subdue such fire or fires and properly protect the property of the inhabitants of said City.

That should such fire or fires occur it would be the duty of the plaintiff under its contract with said City as aforesaid, to furnish to its full capacity water for the purposes aforesaid, and in its failing so to do might make it liable to heavy damages.

Plaintiff further alleges that while the defendants last named herein are not insolvent, they would be unable to respond in damages in an equal amount to the damages which the plaintiff would be liable to sustain, should a destructive fire occur in said City at the present time and while the plaintiff is deprived of a necessary supply of water to fight and control such fire and prevent the destruction of property, by the acts of said defendants in using and diverting the same, and depriving the plaintiff of the use thereof, and that if said defendants were able to respond in damages sufficient to reimburse this plaintiff for damages that might be secured against it as aforesaid, to recover

the same, plaintiff would be compelled to institute and prosecute a multiplicity of suits and actions.

XVI.

Plaintiff further alleges that unless the defendants last herein named are immediately restrained and enjoined from diverting and using the water of said Rattlesnake Creek to the use of **which** the plaintiff is entitled, the plaintiff will suffer great and irreparable injury. That the present supply of water that the plaintiff can now procure for the purpose aforesaid, is so limited, caused by the acts of the said defendants as aforesaid, and for the reason stated as aforesaid, [208] the danger from fire is so imminent, that there is not sufficient time to give defendants notice to show cause why said temporary injunction should not be granted.

WHEREFORE, plaintiff prays judgment:

1st. That the plaintiff be adjudged and decreed the prior right over each and every one of said defendants, to the perpetual use of forty-two hundred (4200) inches of the water of Rattlesnake Creek.

2nd. That each and every one of the defendants named herein, be required to appear and answer, and establish by proof the extent of their interests in the waters of said Rattlesnake Creek, if any they have.

3rd. That upon a final hearing of this action that the Court render a decree determining the rights of all the parties to this action to the waters

of said Rattlesnake Creek, as the same may be made to appear.

4th. That a temporary injunction be immediately issued enjoining and restraining the defendants, Charles E. Williams, John Barett, John Capp, Otto Quast, Mrs. E. J. Clements, William Neil, Jacob G. Ambrose and A. A. Settlemire, and each and every one of them, and each and every one of their agents, servants, attorneys or employees, from diverting or using any of the water of said Rattlesnake Creek, and depriving the plaintiff of the use thereof, until the final hearing of this cause, or until the further order of the Judge of the above entitled Court.

5th. That the defendants, and each and every one of them, be perpetually enjoined and restrained from in anywise molesting or interfering with the water rights of the plaintiff after the same have been determined by this Court. [209]

6th. That the plaintiff be decreed the right to take from said Rattlesnake Creek, at one place, to be by it selected, all of the water of said creek, to which the Court shall find the plaintiff entitled.

7th. Plaintiff prays judgment for costs herein expended, and for all general and special relief.

WOODY & WOODY &
MARSHALL & STIFF

Attorneys for Plaintiffs.

State of Montana,
County of Missoula.—ss.

T. T. McLeod, being first duly sworn upon his oath, deposes and says: that the plaintiff herein

is a corporation, and that he is an officer thereof, to-wit, manager; that he has read the foregoing complaint, and knows the contents thereof, and that the matters therein stated are true to his best knowledge, information and belief, as such manager, except as to the matters therein stated as to the diverting and using of said water by the said defendants, and depriving the plaintiff of the use thereof, and of the promises and acts of the said defendants, and the insufficient supply of water now had by the plaintiff, plaintiff's urgent need of the same, and imminent danger from fires if plaintiff is deprived of said water, the damage the plaintiff is liable to incur if the parties are not enjoined as prayed for, and all of these facts he knows of his own personal knowledge.

T. T. McLEOD

Subscribed and sworn to before me this the 26 day of October, 1901.

HENRY C. STIFF [210]

[Seal]

Notary Public in and for
Missoula County, Montana.

Service, by copy, of the foregoing amended complaint is hereby accepted, this the 26 day of October, 1901.

DIXON & MURPHY

of Attorneys for Defendants.

(Filed: Oct. 26, 1901.)

(Duly certified by the clerk of said court to be a true copy of said amended complaint.)

Mr. WHITLOCK: And I also offer in evidence answer to the amended complaint of Charles E. Williams and Jennie Williams and others.

Mr. WILSON: We have no objection.

DEFENDANT'S EXHIBIT 10,

the answer to amended complaint above mentioned, so admitted in evidence without objection, is in words and figures as follows, to-wit:

[Title of Court and Cause as in Exhibit 9, supra.]

Now come the above named defendants, Charles E. Williams and Jennie Williams. Otto Quast, and Jacob G. Ambrose, and for their separate answer to the amended complaint herein:

DENY each and every allegation therein contained that is not specifically admitted or denied hereinafter.

1. With reference to the allegations contained in paragraphs one (1), two (2) and three (3) of said amended complaint, they deny any knowledge or information thereof sufficient to form a belief.

2. Admit the allegations contained in paragraphs four (4) and five (5) of said amended complaint. [211]

3. With reference to the allegation that the plaintiff is now and for a long time has been the owner of a franchise granted to its predecessors in interest by the common council of the City of Missoula, and the allegation that under and by virtue of such franchise the plaintiff and its prede-

cessors in interest have, at a heavy expense and by the expenditure of large sums of money, laid and constructed water mains and pipes throughout the principal portions of the City of Missoula, these defendants deny any knowledge or information sufficient to form a belief, and therefore deny the same.

4. Admit that plaintiff and its predecessors in interest have diverted and conveyed water from Rattlesnake Creek and supplied the City of Missoula and the inhabitants thereof with water, and is now supplying water to the inhabitants of said City, but deny any knowledge or information sufficient to form a belief as to the allegation that said plaintiff and its predecessors in interest have been diverting, conveying and supplying said water for more than twenty-five years, and therefore deny the same.

5. With reference to the allegations contained in paragraph seven (7) of said amended complaint these defendants deny any knowledge or information sufficient to form a belief, and therefore deny the same, (except that these defendants admit that said plaintiff and its predecessors in interest have diverted and used certain of the waters of said creek.)

6. Admit that these defendants and their co-defendants claim the right to divert and use the waters of Rattlesnake Creek, and for a long time past have been, and now are, diverting and using said waters, but deny that these defendants are now, or have been, diverting or using any water

from said [212] creek to which the plaintiff is entitled as alleged in paragraph nine (9) of said amended complaint, or otherwise, or at all.

7. With reference to the allegation contained in paragraph ten (10) of said amended complaint, these defendants deny any knowledge or information sufficient to form a belief, and therefore deny the same.

8. Deny that these defendants have been, or now are diverting, or will, unless enjoined or restrained from so doing, continue to divert any of the waters of said creek to the use of which plaintiff is entitled by reason of prior appropriation or otherwise, but allege that any diversion of said waters which these defendants are now making, have made, or will in the future make, is by virtue of an appropriation and right as hereinafter stated.

And for further answer to plaintiff's complaint these defendants allege:

1. That the plaintiff asserts and claims a right to the use of certain waters of said creek which have been, and now are being diverted through a certain flume connected with said Rattlesnake Creek a short distance from the mouth of said creek; that the diversion so made is one of the diversions referred to in the complaint herein; that said water so diverted through said flume was for the purpose of furnishing power for a grist mill located on the bank of Hell Gate river, and was used for such purpose for a number of years; that about 10 years ago the use of said water for said purpose ceased

and since that time no use has been made of said water so diverted and through said flume, except for the purpose of furnishing power for certain machinery used in sawing, planing, [213] and otherwise preparing lumber; that for the operation of said machinery the use of only 100 inches of water has been during said time, or is now required, and the plaintiff and its predecessors in interest intend to abandon and have abandoned any right acquired to the use of the waters through said flume, except to the amount of 100 inches.

And these defendants for their further answer, and for a cross-complaint and counter-claim, and for the purpose of stating and setting forth their right to the use of the waters of Rattlesnake Creek, allege:

1. That the defendant, Charles E. Williams, is the owner, in possession, and entitled to the possession of certain lands situated in Missoula County, State of Montana, adjacent to and in the vicinity of the Rattlesnake Creek, and described as follows:

NE $\frac{1}{4}$ of the SE $\frac{1}{4}$ and East half of NW $\frac{1}{4}$ of Section 11 in Township 13 N of Range 19 West, Montana Meridian.

2. That the defendant, Jennie Williams, is the owner, in possession and entitled to the possession of certain lands situated in Missoula County, State of Montana, adjacent to and in the vicinity of the Rattlesnake Creek, and described as follows:

The Northeast quarter of Section 11 Township 13 N of Range 19 West of Montana principal Meridian.

3. That the defendant, Otto Quast, is the owner, in possession and entitled to the possession of certain lands situated in Missoula County, State of Montana, adjacent to and in the vicinity of the Rattlesnake Creek, and described as follows:

SE¹/₄ SE¹/₄; and SW¹/₄ SE¹/₄ less 10 acres; 5 acres in NW¹/₄ of SE¹/₄ of Section 11, and S¹/₂ of SE¹/₄ of SE¹/₄ of Sec. 2 Township 13 N of [214] range 19 West.

4. That the defendant, Jacob G. Ambrose, is the owner, in possession and entitled to the possession of certain lands situated in Missoula County, State of Montana, adjacent to and in the vicinity of the Rattlesnake Creek, and described as follows:

SW¹/₄ of SW¹/₄ of SE¹/₄ of Sec. 11 Township 13 N of Range 19 W. Montana Meridian according to the United States Government survey thereof.

That the defendants H. C. Chattin, John W. Chattin, Charles W. Chattin and Benjamin F. Chattin are the joint owners, in the possession and entitled to the possession of certain lands situated in Missoula County, State of Montana, adjacent to and in the vicinity of Rattlesnake Creek, described as follows: The North three-fourths of the east half of the North-west quarter of the South-east quarter of section eleven township thirteen North range nineteen west, containing about fifteen acres.

That the defendant John A. Kapp is in the possession and entitled to the possession of certain lands situated in Missoula County, State of Montana, adjacent to and in the vicinity of Rattlesnake

Creek described as follows: The South one fourth of the west half of NW $\frac{1}{4}$ of SE of sec. 11 tp 13 N. R. 19 West.

That all of said lands are valuable for agricultural and grazing purposes only, and in order to make the same productive and useful for such purposes irrigation by artificial means is required.

That said defendants in this answer specially named, in the month of April 1st, in the year of 1872, and by their [215] predecessors, who were then the owners and in possession of said land, constructed a ditch with a capacity of 450 inches, connecting with said Rattlensake Creek. That said ditch diverted and conveyed to and upon the above described lands 450 inches of the waters of said Creek, for the purpose of irrigating said lands, and for domestic purposes, thereby appropriating 450 inches of said water.

That the construction of said ditch was commenced on the First day of April in said year, and the work necessary for the completion thereof was prosecuted diligently.

That these defendants, and their grantors and predecessors in interest, have, at all times since said diversion and appropriation, used, enjoyed and possessed as tenants in common, 450 inches of the waters of said Creek, for the purpose of irrigating said lands and for domestic purposes.

That the said waters and the whole thereof so diverted and appropriated as aforesaid, is necessary

and indispensable in and about the irrigation and cultivation of said lands, and in the production of and growing hay, grain, vegetables and grass thereon.

And for further answer to plaintiff's complaint, these defendants allege:

1. That these defendants and their predecessors and grantors in interest have been in the open, notorious, exclusive, continuous and adverse possession, and have had the open, notorious, exclusive, continuous and adverse use and enjoyment of the said 450 inches of the waters of said Creek, for irrigating purposes, during the irrigation season of each and every year since the month of April in the year of 1872, and have during all of said time claimed the right to use and enjoy [216] said water as against said plaintiff, and all others whomsoever.

WHEREFORE these defendants pray that they may be adjudged and decreed the right to use 450 inches of the waters of said Rattlesnake Creek, and of date the 1st day of April in the year 1872, and for their costs and *imbursements* incurred herein, and for such other and further relief as to the Court may seem just and equitable.

CLAYBERG & GUNN

DIXON & MURPHY

W. P. SMITH

Attorneys for Answering Defendants.

State of Montana,
County of Missoula.—ss.

Charles E. Williams, being first duly sworn on his oath says:

That he is one of the defendants named in the foregoing entitled action; that he has read the foregoing answer and knows the contents thereof, and that the matters and things therein stated are true, except as to those things therein stated on information and belief, and as to those things he believes them to be true.

CHAS. E. WILLIAMS

Subscribed and sworn to before me this 10th day of January, 1902.

W. L. MURPHY

Notary Public in and for Missoula
County, Montana.

[Filed: Jan. 10, 1902.]

[Duly certified by the clerk of said court to be a true copy [217] of said answer.]

Mr. WHITLOCK: Counsel have agreed and the record may show that the answers of all of the other defendants in that case are the same as the one I last introduced except as to the description of the land and the description of the water rights claimed.

Mr. WILSON: And the names of the parties. We agree to that.

Mr. WHITLOCK: If your Honor please, I now offer in evidence a certified copy of the first recorded notice of appropriation of the old Mill right.

Mr. WILSON: That is objected to upon the ground that it is—this subject was entirely covered and adjudicated by the decree in 1953, and may not now be impeached or contradicted or collaterally attacked.

Mr. WHITLOCK: It is offered for this reason: it is followed by two other exhibits similar in character which show the history of that particular right and show an intent or declaration of change of place of use of the old Mill right by the appropriators.

The COURT: It may go in for whatever consideration it may be entitled to. Objection overruled.

Mr. WILSON: Exception.

DEFENDANT'S EXHIBIT 11,
the notice of appropriation above mentioned, so admitted in evidence over the objection of the plaintiffs, is in words and [218] figures as follows, to-wit:

WATER RIGHT

Worden & Company, Claimants.

TO ALL WHOM THESE PRESENTS MAY
CONCERN:

KNOW YE, that we, C. P. Higgins and F. L. Worden, doing business in the town of Missoula

Mills, Montana Territory, under the name and firm style of Worden & Co., claim and have appropriated for mill purposes, all the water of Rattlesnake Creek, said water being conveyed by means—dams, ditches and flumes, from a point on said Rattlesnake Creek, about one-third of a mile above the mouth of the same, and where their dam is now located, to the flouring and saw mills, located in the town of Missoula Mills, Missoula County, Montana Territory, said water being claimed and appropriated for the above named purposes to the exclusion of all other claimants.

WITNESS our hands this 16th day of November, A. D. 1868.

C. P. HIGGINS

F. L. WORDEN.

Filed Nov. 16th, 1868, at 2 o'clock P. M.

F. H. WOODY.

County Recorder, Missoula County, M. T.

[Duly certified by the county clerk and recorder of Missoula County, Montana, to be a true copy of said water right, as the same appears on record in his office.]

Mr. WHITLOCK: I now offer Defendant's Exhibit 12, declaration of appropriation of water of Frank L. Worden and Christopher P. Higgins to the Mill right in 1885, and showing the change of point of diversion of that right. [219]

Mr. WILSON: It is objected to upon the ground that it is incompetent, irrelevant and immaterial,

and an attempt to modify, impeach and collaterally attack the decree in cause No. 1953.

The COURT: Of course, it can't do that. Admitted over the objection.

Mr. WILSON: Exception.

DEFENDANT'S EXHIBIT 12,

so admitted in evidence over the objection of the plaintiffs, is in words and figures as follows, to-wit: B—126.

DECLARATION OF APPROPRIATION AND CLAIM TO WATER.

We, Frank L. Worden and Christopher P. Higgins, partners, under the firm name and style of Worden & Co., citizens of the United States, and residents of the town of Missoula, County of Missoula, Montana Territory, do hereby give notice to all persons concerned, that we have heretofore claimed and appropriated all the waters of Rattlesnake Creek in said Missoula County, Montana Territory as follows to-wit:—First, all the waters of said Rattlesnake Creek in Missoula County, Montana Territory. The said waters was and is conveyed by means of dams, flumes and ditches. 2nd, that the purposes for which said water is and was claimed and appropriated for Milling and power purposes, etc., to furnish a water power to run the grist and flouring mill of the above named Worden & Co., situated in the town of Missoula Mills, Montana Territory. That the means of diversion of said

water is by putting in a temporary dam in the main creek when the water is at a low stage, which turns the water into a branch of said stream or main Creek, then by a headgate and flume six (6) feet wide, four (4) feet deep, [220] twenty-four (24) feet long, leading into a ditch of about same dimensions, in width and about one half of a mile long. The capacity of said ditch and flume is about twenty five hundred (2500) inches miners measurement, and carries all the water that flows in said Rattlesnake Creek during the months of September, October, November, December, January and February, when not diverted by ice or other obstructions from said flume and ditch. A record of the appropriation of all of said water in said Creek was made by the said Worden & Co. on the 16th day of November, A. D. 1868, and is recorded in Book (A) of record page 29, records of water rights, in the Records Office for Missoula County, Montana Territory. The name of the stream from which the diversion of said water is made is, as above stated, Rattlesnake Creek. The point where said water is diverted from said stream is about one third of a mile above the mouth of said Creek, where it empties into the Hellgate River. That in the year 1868, there being at certain portions or months of the year when said creek is at a higher stage of water, a surplus in said Creek, over and above the water diverted for said Milling purposes, as hereinbefore described, and when the said waters were not so required for Milling purposes, under the said appropriation, Christopher P. Higgins di-

verted a portion of said surplus, at such times as there should be a surplus, for irrigating, mechanical, and other useful purposes, and recorded said notice of appropriation on the 16th day of November, 1868, which is recorded in Book A page 30, of water rights and locations, in the County Recorders Office, Missoula County, Montana Territory. The undersigned do hereby further give notice that they claim and have heretofore claimed from the surplus water in said Creek, [221] when there shall be a surplus in said Creek, over and above the waters hereinbefore mentioned and described, as diverted and appropriated, one hundred inches, or so much of said water as shall be required and sufficient for the purposes hereinafter mentioned and described. That the purposes for which said last above mentioned diversions claim and appropriation is claimed, is for the purpose of furnishing the Missoula Water Works with a sufficient supply of water to supply the town of Missoula and the citizens thereof with water for irrigation, household and domestic purposes. That the date of the appropriation of said last above mentioned water is and was in the year 1871. That the means of diversion of said last above mentioned water is by putting a dam in the branch of said Creek, to which the water is diverted by the ditch of C. P. Higgins, heretofore mentioned, then a flume or box, about 18 x 24 inches, with two screens at the head with a head gate in said flume, about ten inches square, with a head of water over said head gate of about eighteen

inches, supplying the boxes, reservoirs, and pipes of the Missoula Water Works, with one hundred inches or more of water, miners measurement. That in the years 1881, 1882, 1883, 1884, new flumes, boxes, reservoirs, iron pipes, and a permanent head gate in the main Creek was put in, in order *to a* more permanent and sufficient supply of water for said water works and to said Town. The date of the appropriation of said last mentioned water was in the year 1871, and the said Frank L. Worden and Christopher P. Higgins, partners, under the firm name and style of Worden & Co., are and were the appropriators and are the present owners of all of said water, as above mentioned. The name of the stream from which said water is diverted is Rattlesnake Creek. [222] That the point where said water last above mentioned is diverted from said Creek is at the same point where the water mentioned as having been appropriated by said C. P. Higgins is diverted, and is about one and one half ($1\frac{1}{2}$) miles above the mouth of said creek, on its West bank, in Missoula County, Montana Territory. That this declaration and claim of all said water as above mentioned is made to comply with the Act of the Legislative Assembly of the Territory of Montana, relative to water rights, approved March 12, 1885, and is made without waiving any rights by virtue of prior claims and appropriations.

WITNESS our hands this 20th day of June, A. D. 1885.

FRANK L. WORDEN.

CHRISTOPHER P. HIGGINS.

Territory of Montana,
County of Missoula.—ss.

Frank L. Worden and Christopher P. Higgins, being duly sworn on their oaths, deposes and says: That they are members of the firm of Worden & Co., the persons mentioned in the foregoing notice of prior appropriation and claim of the waters therein mentioned; that he has heard the same read and know the contents thereof and that the said notice is true of their own knowledge.

FRANK L. WORDEN.

CHRISTOPHER P. HIGGINS.

Subscribed and sworn to before me this 20th day of June A. D. 1885.

[Notarial Seal] THOMAS C. MARSHALL,
Notary Public.

Filed June 20, 1885, at 4 P. M. [223]

(Duly certified by the county clerk and recorder of Missoula County, Montana, to be a true copy of said declaration of appropriation, as the same appears on record in his office.)

Mr. WHITLOCK: I now offer as the Defendant's Exhibit 13 a similar copy notice of water right by the—relating to the same right, showing a change of diversion at a later date, this one bearing the date 1887.

Mr. WILSON: The same objection as was made to Exhibit 12.

The COURT: A like ruling.

Mr. WILSON: Exception.

DEFENDANT'S EXHIBIT 13,

so admitted in evidence over the objection of the plaintiffs, is in words and figures as follows, to-wit:

NOTICE OF WATER RIGHT

B—273

Territory of Montana,
County of Missoula—ss.

To all whom these presents may concern:

Know ye, that the undersigned, a corporation organized and existing under the laws of Montana Territory, do hereby publish and declare, as a legal notice to all the world, that we, have a legal right to the use, possession and control of and claim two thousand (2000) inches of the waters of Rattlesnake Creek in said County and Territory, for milling, mechanical, and other useful purposes, including the supplying of the town of Missoula with water.

That we have diverted the said water from the main chan- [224] nel of Rattlesnake Creek, at a point upon its West bank, on the land claimed by W. A. Clark, near the North line of the same, and about $\frac{1}{2}$ mile above the residence of said W. A. Clark, by means of a headgate, which said headgate is sixty (60) inches wide by forty-eight (48) inches deep in size, and carries 2000 inches of the water aforesaid into a West branch of Rattlesnake Creek. This point of diversion is further marked and designated as being a little East of a large pine tree about 4 feet in diameter, standing on the bluff on the West side of said Creek, and marked and blazed. That at a

point about six hundred feet below and south of this point of diversion we take and divert the water from the said West branch of Rattlesnake Creek by means of a dam and a headgate which said headgate is sixty (60) inches wide by forty-eight inches deep in size, and which carries and conducts said 2000 inches of water into a ditch made of boxes, eighteen inches by twenty-four inches in size, covered with earth, which said covered ditch runs in a southerly direction about 2-6/10 miles to a reservoir upon the hill North of Missoula, thence to any requisite point of discharge. That this notice of location and claim is intended as an amendment to two certain water rights made by Frank L. Worden and Christopher P. Higgins one of which bears date of November 16th, 1868, and is recorded in the office of the County Recorder of Missoula County in Book A. of water rights page 29, the other water right being made by the same parties on June 20, 1885, and recorded in the office of the County Recorder of Missoula County in Book B. of Water Rights, on pages 126, 127, 128, 129 and 130, and is a change of the point of diversion of the water claimed under said notices, in accordance with the provisions of Section 3 [225] of an Act relative to Water Rights, passed by the Fourteenth Legislative Assembly of Montana Territory and approved March 12, 1885. Reference is hereby made to said records for a further description. That the undersigned corporation is the legal owner of said water and water right by means of purchase.

That we also claim said ditch and the right of way thereof, and for the water by it conveyed, or to be conveyed, from said point of appropriation to said point of final discharge, and also the right of location upon any lands of any dams, flumes or reservoirs, constructed or to be constructed, by us in appropriating and using said water. That we also claim the right to keep in repair and enlarge said means of water appropriation at any time, and the right to dispose of said water, ditch, right, or said appurtenances, in part or whole at any time.

CLAIMING THE SAME ALL AND SINGULAR under any and all laws, National and Territorial, relating to water rights, and specifically under Sections 271, and 272, 731 to 735, inclusive, and 738 and 741, General Laws of Montana, Revised Statutes of 1879 or as amended, and particularly under an act of the Fourteenth Legislative Assembly of Montana Territory, approved March 12, 1885. Together with all and singular the hereditaments, and appurtenances thereunto belonging or in anywise appertaining.

Signed for the Corporation by its President at Missoula, Montana Territory, this 26th day of July, A. D. 1887.

MISSOULA WATER WORKS AND
MILLING COMPANY

By C. P. Higgins, President.

Territory of Montana,
County of Missoula.—ss. [226]

C. P. Higgins being duly sworn deposes and says that he is the President of the Missoula Water Works and Milling Company, the corporation named as the locator and claimant, of the within named and described water right; that he knows the contents thereof, and that the matters and things therein stated are true of his own knowledge.

C. P. HIGGINS

Subscribed and sworn to before me this 27th day of July, 1887.

[Seal]

ALVIN LENT,
Notary Public.

I certify that I received this instrument for record on the 27th day of July, 1887, at 4:30 o'clock P. M.

ALVIN LENT,
County Recorder

Filed: July 27th, 1887, at 4:30 P. M.

PETER FEDDERSON,

a witness called in behalf of the defendant, having been first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Pope:

The WITNESS: My name is Peter Fedderson; I reside in California, but formerly resided in Missoula County; I came here in 1879 and I left

(Testimony of Peter Fedderson.)

in 1910. During that period of time I owned and operated a ranch located on Rattlesnake Creek. I was a party to the action which has been referred to here as the suit brought by the Missoula Water Company against Williams and others for the purpose of adjudicating the rights in Rattlesnake Creek; I was a defendant in that action. I re- [227] call that that suit was commenced in the neighborhood of 1902, but I thought it was sooner.

With reference to the commencement of that suit, I can state where the supply of water for supplying the city of Missoula and its inhabitants was taken out; it was about a quarter of a mile—probably not that much—I should say an eighth of a mile below the barns—below my barn. Referring to the map, Exhibit 6, and to the point where it is marked “water works,” that is approximately the location of the head of the ditch or flume for supplying the city of Missoula at that time. At that time I don’t think there was any other point or place from which the city of Missoula or the water company furnishing the city of Missoula with water was obtaining a supply of water for that purpose.

I am familiar, of course, with the old Mill ditch. Prior to the commencement of the suit there was not any more appreciable use being made of the Mill ditch than what I heard here today telling—told by people that used it for carpenter shop, Mr. Newton and others. I knew of it being used for some time to supply Mr. Newton with power. As to the Higgins ditch, there was not a great deal of

(Testimony of Peter Fedderson.)

use being made of that prior to the time the suit was commenced. I couldn't fix a date which was the last date when the old flour mill was used, but I think it was—I had a lot of barley ground and dried at the time the Missoula brewery burned down, and while they was trying to put out the fire they had a lot of barley that was lying in vats. I think that was in 1891 or '2. As to whether there was any use ever made of the flour mill after that date, well, there may have been some time a year or so. They tried to grind some flour or oatmeal or something of that [228] kind, but not to a great extent.

As to what occurred in regard to the old flume that I have described as originating approximately an eighth of a mile below my barn prior to the time the point of diversion for the city water supply was put upstream, and what was the occasion for moving the headgate upstream, well, for years there they have tried to do away with the filth of the barnyard. There was 100 or 125 head of cattle there, and in the spring of the year when the snow went off it naturally made a lot of slush and stuff and it run down in that channel where they took the water out into the flume that diverted the water, and that was several years before—that condition existed several years before they moved the diversion of that water. That flume was a box flume, covered.

I think it was in '92 that the place of diversion of the city water supply was moved upstream—1902.

(Testimony of Peter Fedderson.)

At that time a pipeline was laid under the ground from the new point of diversion; that crossed my land. That ran along the slope of the hills above the house. I don't know if the line of that pipeline was readily noticed by anyone in the valley; it was buried but it could be seen if they had an idea of looking and wanted to see it; it was easy to be seen.

I was myself irrigating my land there at the time that the suit was brought; and also at the time that the point of diversion was moved upstream to the present location I was irrigating and farming. My ditch took out of the stream right below the present dam—right about the length of this room. I don't think that I noticed any diminution of the supply available for irrigation after the dam was put up there compared to the supply available before that. [229]

Q. What would you say about the development of irrigation in the Rattlesnake valley as to whether up until the year 1887 there was any considerable amount of irrigation and farming by irrigation in that valley?

Mr. WILSON: That is objected to upon the ground that the rights for irrigation or otherwise of the waters of Rattlesnake Creek have been fixed by the decree in cause No. 1953, and cannot be impeached or collaterally attacked.

The COURT: Well, that is probably true as to the extent of the rights. Perhaps it is not very

(Testimony of Peter Fedderson.)

material. If not material or entitled to consideration the Court will give it none. Overruled.

Mr. WILSON: Exception.

A. We used—what did you mean?

Q. The question was how extensive was irrigation in the Rattlesnake valley up to 1887?

A. Very little.

The WITNESS: I think it was in 1894 or '5 that considerable irrigation commenced there after that. Some subdivisions—a man that came in there, named Cobban, and others came in there and laid out subdivisions and acquired water rights.

Q. Now, at the time that the suit was started—I mean the suit in which you were a defendant—did you know at that time of any intended change in the point of diversion of the water works there?

Mr. WILSON: Just a moment. That is objected to upon the ground that it is incompetent, irrelevant and immaterial and self-serving and hearsay—[230] not a fact in issue in this case.

The COURT: It may be entitled to no consideration. The Court will allow him to speak, and if not, the Court will ignore it.

Mr. WILSON: Exception.

A. It was told me they did.

Mr. WILSON: We move to strike the answer out as hearsay.

The COURT: Overruled.

Mr. WILSON: Exception.

(Testimony of Peter Fedderson.)

CROSS EXAMINATION by Mr. Mulroney:

The WITNESS: I sold out to the water company in 1910; that is, I transferred my place to the water company, and also the water rights. I don't know as to the date of 1910; I think it was a little sooner. I think that the change from the lower place to the upper wasn't made until June of 1902. I had heard that they proposed to make a change prior to that time. They hadn't, up to the 13th of August, 1901, which was the date of the filing of the complaint in suit 1953, to which I was a party, made the change at all. I don't think they had done anything at all to change the point from the old place to the new.

Witness Excused.

J. M. PRICE,

a witness called in behalf of the defendant, having been first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Whitlock:

The WITNESS: My name is J. M. Price; I reside at Los Angeles, California, but was formerly a resident of this [231] county. In the year 1906, to which my attention is directed, I had something to do with Rattlesnake Creek; I was water commissioner. I am not positive what period of time during that year my duties in that capacity covered, but I think I was on there about 80 days. At that

(Testimony of J. M. Price.)

time I measured out and delivered water to the company which was then supplying the city of Missoula with its water supply.

I am familiar with the present point of diversion of the supply for the city of Missoula. The point of diversion at that time was the same as it is at present. In 1906 I delivered to the water company supplying the city of Missoula the supply which it required for that purpose from the dam where it is being delivered at the present time. I did not deliver to that company any water at the head of the Mill ditch. I had nothing whatsoever to do with the old Mill ditch at that time.

CROSS EXAMINATION by Mr. Mulroney:

The WITNESS: Handed a report made by me in that year as the water commissioner, being file number 68 in cause No. 1953, the signature which is a part of that report is my own. I couldn't tell you offhand to what ditch I referred as the Hammond ditch, or what ditch is the Hammond ditch. I couldn't say for sure without looking at the decree whether it was the Mill ditch. Doesn't it mention it in the decree. I think that Hammond did not own the Mill ditch. It originally belonged to Worden and Higgins; Hammond may have bought it afterward; I don't think he did.

I also made a charge of the distribution of water into the Higgins ditch, which counsel sees there. That was in 1906. [232] Frankly, I can't recall what this other one is here, the Hammond ditch.

(Testimony of J. M. Price.)

I refer to the Hollenbeck, the Quast, the Effinger, the Williams; I know about those ditches; they are the same. The Kemp, the Cobban, the Higgins, the Hamilton-Day ditch, Fedderson, Fredline, the water company—we understand about all of those but the Hammond ditch. I presume that it was the Mill ditch, but I couldn't say because I don't know.

REDIRECT EXAMINATION by Mr. Pope:

The WITNESS: I am familiar, of course, with the ditch which leads down to what we call the Hughes gardens and which is shown on the map as the Fredline ditch. My attention being called to that ditch and my recollection being refreshed, I think it is possibly correct that I know what the Hammond ditch was. I remember now that was known as the Hammond ditch; I think that is correct. I think it is correct that it is the one that is called the Fredline ditch.

Q. Your recollection is, Mr. Price, that you had nothing whatsoever to do with the Mill ditch?

Mr. MULRONEY: That is objected to as leading.

The COURT: Well, it is, but he has already said, and it is an effort to reaffirm it. The objection is sustained.

Witness Excused.

G. J. HAGENS,

a witness called in behalf of the defendant, having been first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Whitlock:

The WITNESS: My name is G. J. Hagens; I reside at Ham- [233] ilton, Montana. My business is that of civil engineer. The experience that I have had in engineering as the same applies to water rights is irrigation for about the last 15 years. I have a connection with an irrigation system at the present time—with the Bitter Root irrigation system; I have been connected with that system for 14 years. That system has a length of 72 miles and irrigates about 20,000 acres.

I am familiar with the creek known as Rattlesnake Creek. At the request of counsel for the defendant I have made an examination of that creek; I have gone along the creek from the location of the dam to the mouth of the stream.

Q. And I will ask you if you were able to determine from your examination of the stream and from your experience in that kind of work and in irrigation—did you determine whether or not there were any additions to the flow of this stream from the point of the defendant's dam down stream?

Mr. WILSON: We object to that as not a subject upon which an opinion may be expressed, and it is not any fact involved——

The COURT: He is not asking for an opinion. He has asked him if he was able to determine

(Testimony of G. J. Hagens.)

whether there were any accretions to the stream below the dam. Overruled.

Mr. WILSON: Exception.

A. Yes, I was able.

The WITNESS: I say that there are not any such accretions. I made a sufficiently thorough examination to satisfy myself on that point.

Q. Now, assuming, Mr. Hagens, having in mind that particular stream and having in mind the place where it reaches Pine [234] Street, which is the approximate location of the old Mill ditch—assuming now that you were advised that water was observed and measured in that stream at that point in an amount of 200 or in excess of 200 inches at a time when stretches of the stream above that point and between that point and the dam of the defendant were approximately dry, if not altogether so, what, from your experience and observation of the stream, would you say is the explanation of the presence of water there?

Mr. WILSON: That is objected to upon the ground that it is not a subject upon which an opinion may be expressed, and not calling for any fact involved in this case.

The COURT: I think that is a matter of opinion about which you may argue and that is about all. I can't see how opinions can help you any.

Mr. WHITLOCK: Well, I think certainly the action of water and what is to be expected of it is the proper subject of expert opinion.

(Testimony of G. J. Hagens.)

The COURT: Well, here is, you say, 200 inches of water at the head of the Mill ditch?

Mr. WHITLOCK: Yes sir.

The COURT: And how far above is that dam?

Mr. WHITLOCK: Something over two miles—three miles.

The COURT: And below it it is dry, you say. Why, it is inescapable. You don't need any witnesses to tell me that that water came in from some place below there—rose in the bed.

Mr. WHITLOCK: Well, it is our idea that it would not come from elsewhere, and I think the testimony [235] if permitted will bear us out.

The COURT: If the stream was dry below there, that this water seeped in below and rose in the bed is inescapable. I would not take the word of any witness otherwise.

(The objection was argued by counsel.)

The COURT: That is a mere guess. As I say, it may be argued, but the opinion of one witness is not better than another. Objection sustained.

Mr. WHITLOCK: May I state an oral offer of proof?

The COURT: You may.

Mr. WHITLOCK: The defendant offers to prove by the witness on the stand that if permitted to answer he would say in answer to the question asked that the water appearing at that point is in fact creek water which has passed over the dam and which goes into the bed of the stream and arises at the points along below.

(Testimony of G. J. Hagens.)

Mr. WILSON: The same objection to the offer.

The COURT: Sustained. If it went over the dam there would be witnesses to the fact. It would not require an expert.

Mr. WHITLOCK: Exception.

Q. Mr. Hagens, from your examination of that stream and your knowledge and experience in your line of work, I will ask you to assume that you desire to deliver, we will say, 946 inches of water from the stream at two possible points of diversion, the Mill ditch, which is at Pine Street, and the point immediately above the dam of the defendant company; and assume that between those two points there are other users who take out [236] water through ditches for agricultural purposes, and also others who take out for similar purposes above the dam. I will ask you at which point, in your opinion, could you deliver the 946 inches, as between the two points that I have mentioned, and at the same time leave in the stream available for use the greater amount of water for the other users from the stream?

Mr. WILSON: That is objected to upon the ground that it is not a proper subject for the expression of opinion by the witness; it is a fact in issue which must be determined by the Court from the testimony as to the facts given by the witnesses.

The COURT: Well, you are assuming there is no other water coming into the stream but from the dam?

(Testimony of G. J. Hagens.)

Mr. WHITLOCK: That is correct.

The COURT: Well, you don't need any answer to that. I will say you could take it out to the best advantage above to escape evaporation. You don't need any opinion on that. Sustained.

Mr. WHITLOCK: Exception.

CROSS EXAMINATION by Mr. Mulroney:

The WITNESS: Asked to assume that above the dam indicated upon the map here water is taken out of the Effinger ditch, the Quast ditch and other ditches along there to the extent of 400 or 500 inches; that it is spread out upon the land at a point below the point of the dam in order to irrigate the crop; and having in mind my observation of the fact that the mountain is to the east from a half mile to a mile [237] and that there is a rather sharp slope from the mountain back to the creek; and being asked to state from my experience and observation where I would say that 400 or 500 inches would actually go after it is placed upon the land: I will say that you give me one condition there that doesn't exist, and that is the land doesn't slope from the east side toward the creek; it slopes in a southerly direction toward the river. If you will modify that I can answer it. Answering it, I will say that the line of seepage would be in a southerly direction toward the river, and possibly there is a deep gravel deposit there that doesn't reach the water at all. At any rate, my answer would be that from my actual observation of the

(Testimony of G. J. Hagens.)

creek and the valley and the mountain, the slope, that that 400 or 500 inches might get back to the creek to a very small extent—whatever could get away if there was enough water put on the ground at any time. My idea is that it goes in the ground and toward the south of the river, unless there was sufficient water to fill that gravel reservoir to overflowing; in that case it might outcrop pretty near the surface of the creek.

REDIRECT EXAMINATION by Mr. Whitlock:

The WITNESS: If the water did not seep in from the irrigation, as suggested to me by Mr. Mulroney, I would say that it would come from the bed of the stream, having come in from the stream at some point above. Dealing with a larger volume of water it would undoubtedly fill that reservoir of loose boulders underneath and outcrop in places. In order to maintain any uniformity in amount at the point below, it would be necessary to maintain the supply above and upstream.

Witness excused.

[238]

Mr. WHITLOCK: We have a couple more engineers, your Honor, we expected to put the same questions to as to this witness. And I think in view of your Honor's ruling it is not necessary.

The COURT: Very well.

W. L. MURPHY,

a witness called in behalf of the defendant, having been first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Whitlock:

The WITNESS: My name is W. L. Murphy. I am of counsel in this case. I am acquainted in a general way with the water works system which furnishes Missoula. I have no information about the preparations that were made for the location of the dam at the present point, having in mind particularly the acquisition of the site for it, except information from the record which is found in the clerk's office of the district court of this district, and I have only learned that recently so that no certified copy of it could be prepared. I have that original record here; it is in that case on the table there.

It is a proceeding in eminent domain in which the Missoula Water Company is plaintiff and James S. Kemp or J. S. Kemp is defendant, being the same plaintiff as in case No. 1953. The land sought to be condemned is the land upon which the dam and creek reservoir of the Missoula Water Company at that time was to be located and is now located. The date of the institution of that proceeding is in June of 1901; I don't remember the exact time. The original file is there that you might present it to counsel.

I am familiar with the parties to the old water right [239] suit the decree in which has been introduced in evidence; I know the names of the parties.

(Testimony of W. L. Murphy.)

Q. What have you to say as to whether some or many of those people are here and available.

Mr. WILSON: We object to this, if your Honor please, and to this line of testimony upon the ground that the matters involved or that could be involved in that litigation were all matters in issue in cause No. 1953, which has been concluded by a decree which cannot be impeached or collaterally attacked or——

Mr. WHITLOCK: It bears solely on the question of laches.

The COURT: Overruled.

Mr. WILSON: Exception.

A. I have a recollection and have refreshed that recollection in various ways so that I am sure that certain men testified in that case concerning the water rights involved in that case, and of those men I have jotted down the names of many that I remember who are dead; the name of——

Mr. WILSON: We object to counsel stating the names of the witnesses because that would be a matter which could be shown only by the record in the case and counsel's recollection would not be the best evidence.

The COURT: Is the record here?

The WITNESS: Asked what I have to say as to the record in the case as to the witnesses or evidence, and what effort I have made to obtain that, I will say that I have many times searched for a record or transcript of the testimony in the case, and that I have been unable to find, and after

(Testimony of W. L. Murphy.)
inquiry [240] of the clerks they have been unable to find any. However, there are certain minute entries made by the clerk in which the names of certain witnesses for the parties appear, but in practically all of those cases the clerk or someone has run a line through the minute entry containing the names of the witnesses. They are legible and can be seen but apparently are not a part of the clerk's minutes. That can be observed by the original judgment roll which is on the table before counsel for the plaintiffs.

Q. Well then, those persons, as you have examined those names—what has become of them? Are they available?

The COURT: Where has he got his information?

Mr. WHITLOCK: I am asking him for his own knowledge now.

The COURT: Witnesses he knew?

Mr. WHITLOCK: Yes.

A. Only as to witnesses that I knew.

The COURT: And at the time you yourself were present?

A. Yes.

The COURT: Oh, I think he may answer. I can't see it is very material.

Mr. WILSON: Exception.

A. The witness W. T. Hamilton is dead; the witness Father Palladino is dead; Thomas C. Marshall, who was a witness and one of the counsel in the case is dead; J. H. Harper I don't know.

(Testimony of W. L. Murphy.)

Alfred Cave, who was a manager of the water company, is dead; J. H. T. Ryman, who was a witness, is dead. Peter Fedderson was a witness; he has been here. C. E. Williams—I have endeavored to locate him and I have no knowledge as to whether he is living or dead, but I couldn't locate him. E. W. Schilling, a witness, is dead; Samuel Park, a witness, is [241] dead; H. A. Chaney, a witness, is dead; Herman Hutter, a witness, is dead; Ben Hanraher, a witness, is dead; and William H. Reed, a witness, is dead. Those are all the witnesses that I know and know that they are dead.

The WITNESS: I was present at the time of the trial.

CROSS EXAMINATION by Mr. Mulroney:

The WITNESS: I would know only by recollection the other witnesses besides those that I have already told you of. Of those that I remember, there is a Mr. Bain, who was the chief engineer, I think, for the plaintiff in the case; and there was George K. ———, who was the chief engineer for the defendants in the case. As to whether I don't remember the others, I don't know whether they are living or whether they are dead, but I know some of them. I recall others who are here besides Mr. Fedderson—Elmer Hughes, who was mentioned here this morning. As to whether there are any others offhand that I recall, I have made just these notes; I can take the record and——

The COURT: I understand there was no record.

A. Well, I explained to the Court that the names

(Testimony of W. L. Murphy.)

of the witnesses who testified in that record, in most instances there is a line drawn through them and they are evidently taken out by the clerk as of the record in this case. They are legible and can be read.

REDIRECT EXAMINATION by Mr. Whitlock:

The WITNESS: When I referred to the record you were not to understand me to be referring to a transcript of the testimony in the case. There is a record of minute entries which [242] shows the names of the witnesses who were called and examined in the case, but in nearly every instance you will observe a red line drawn in both directions through the names. That means evidently that they are not part of the official record.

RECROSS EXAMINATION by Mr. Mulroney:

The WITNESS: I have no information at all as to who actually drew the lines, but it is in the official file.

The COURT: What is the object anyhow of this?

Mr. WHITLOCK: Just bearing on the question of laches is all.

The COURT: Whose laches?

Mr. WHITLOCK: The laches of the plaintiffs in this case in bringing the matter to issue at a time when the witnesses had died.

The COURT: This is in the same suit?

(Testimony of W. L. Murphy.)

Mr. WHITLOCK: The same people who would know about this question of changing the point of diversion, whether it was considered at that time or not.

The COURT: Very well; proceed.

Mr. WHITLOCK: The judgment roll not disclosing that question.

Witness excused.

H. S. THANE,

a witness in behalf of the defendant, recalled for further examination, testified as follows:

DIRECT EXAMINATION by Mr. Whitlock:

The WITNESS: Assuming that the dam is constructed in the Rattlesnake on bedrock, I would say that there is very slight [243] probability of water seeping under that dam. It is a tight dam, to the best of my knowledge and belief.

Witness excused.

Mr. WILSON: There was just a point. We had agreed that the Court might deem that the value of the amount in controversy in this case exceeds three thousand dollars, so we offered no testimony on the point and came near forgetting it.

Mr. WHITLOCK: That may be agreed.

The COURT: Very well.

Thereupon, the hour of 5:00 o'clock p. m. having arrived, the court was in recess and further trial of said cause was continued until Thursday, October 26th, 1933, at 9:30 o'clock a. m. [244]

J. C. SAIN,

recalled for further cross examination, and testified as follows:

CROSS EXAMINATION by Mr. Whitlock:

I participated in placing a weir and measuring the water at a point above defendant's dam, but forget the year and I cannot recall whether it was at the time of the measurements down at Pine Street or not.

ARTHUR STICHT,

called as a witness on behalf of the defendant, being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Whitlock:

My name is Arthur Sticht; I reside in Missoula. In 1926, I made measurements to determine the flow of Rattlesnake creek at a weir placed in the creek above Effinger bridge, above defendant's dam. The weir was placed there at the request of Rattlesnake Irrigation Company committee. I made notes of the measurements and now refer to such notes. The placement of the weir was completed at 4:00

(Testimony of Arthur Sticht.)

P. M. August 7, 1926, and the measurement found to be 892 miners inches; on August 8th at 1:00 o'clock P. M. the measurement was 909 miners inches; on August 8th at 3:00 o'clock P. M. 909 miners inches; on August 9th at 3:00 o'clock, 975 inches; August 11th at 10:15 A. M. 1031.8 miners inches. There was supposed to be lake water turned in before this last measurement.

CROSS EXAMINATION by Mr. Mulroney:

The weir was approximately 100 yards above the Effinger bridge, which is below the intake of the Effinger ditch and the Franklin ditch is above that, way up, which is the only higher up ditch I know of. The weir was installed by the Rattlesnake people, myself included. Those actually constructing [245] it were E. E. Warner, J. C. Sain, none of whom were engineers. It was a ten foot weir and the whole stream went over the weir. On August 8th, the measurement was 909 inches. The depth of water over the crest of the weir at that date was $9\frac{1}{4}$ inches.

REDIRECT EXAMINATION by Mr. Whitlock:

The Mr. Sain, who helped construct the weir, is the Mr. Sain who just preceded me on the witness stand. According to the decree, the Effinger right was for 100 inches.

RECROSS EXAMINATION by Mr. Mulroney:

Where we measured is about the point marked "Effinger Bridge" on defendant's Exhibit 6 and

(Testimony of H. S. Thane.)

Spring creek comes into Rattlesnake below that, and was flowing approximately 40 or 50 inches.

H. S. THANE,

called as a witness on behalf of the defendant, being first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Whitlock:

I have previously testified in this case.

Q. I want you to assume the following, Mr. Thane,—assume that you have a stream bed in which some of the water sinks and reappears in the bed of the stream at a lower point, and assume that in order to furnish a given flow of water below the point of reappearance it is necessary to maintain a stream of flowing water over the bed last described,—is it possible, in delivering such amount of water, to get any benefit from any such water which sinks and reappears?

A. No there is not.

Mr. WILSON: We object. It isn't a proper subject of opinion evidence and is incompetent, irrelevant and immaterial and is a matter that must be de- [246] termined by the Court as a fact.

The COURT: You mean where the sinking and reappearance would be constant?

Mr. WHITLOCK: Yes, if your Honor please,

The COURT: He may answer it. I think it is self evident. The objection is overruled.

A. No it is not possible to get any benefit at the lower point.

(Testimony of H. S. Thane.)

That is because if any water rises after sinking, it must be immediately replaced at the upper point where it sank, which must be from the flowing stream.

A. That replacement would be from the flowing stream. Of course if any water passes from the bed it would be immediately replaced.

The COURT: In other words, two and two make four?

A. Exactly. You can't add anything to the creek.

The COURT: Proceed.

Q. And on such a stream as I described in the last question, what happens with reference to the sinking and reappearing water when the flow is cut off above?

Mr. WILSON: Objected to. No such opinion can be expressed.

The COURT: The Court, if it is entitled to no consideration, will give it none. For the sake of the record, your objection is overruled.

A. In such a situation the flow at the lower end would continue for some time but at a decreased rate, and would finally stop.

Q. Now in view of your answers to the two preceding questions, if you assume in this case this,—we will say 200 inches of water which has sunk at some point above in the bed of the stream, re-appears at Pine Street, that is, the head of the Old Williams [247] ditch, the old mill ditch,—how much water would you have to let down at a point

(Testimony of H. S. Thane.)

above to deliver 946 inches continuous flow at the mill ditch, if you assume that you are to make no deduction for loss on the way?

Mr. WILSON: Objected to. It is not a matter on which the witness has shown any qualification to express an opinion, if an opinion can be expressed, in any case, and is wholly immaterial.

The COURT: Where is your evidence that 200 inches sinks above?

Mr. WHITLOCK: I am using the figures of the plaintiff.

The COURT: For the sake of the record,—if it is entitled to no consideration the Court will give it none,—the objection is overruled.

Mr. WILSON: Exception.

A. I think it is obvious that it would take 946 inches.

CROSS EXAMINATION by Mr. Mulroney:

My answers are based on the assumption that there isn't any other water coming into the stream from the west at all.

Mr. WHITLOCK: We have, if your Honor please, and offer in evidence a certified copy of the complaint referred to in the testimony yesterday, in the case of Missoula Water Company against J. S. Kemp, being the complaint in the condemnation proceedings.

Mr. WILSON: To which we object on the ground that it is immaterial and throws no light on the issues involved in this case.

(Testimony of H. S. Thane.)

The COURT: What is the object?

Mr. WHITLOCK: It will show, if your Honor please, that long before this suit, that the matter was known and [248] a matter of public record, that preparations were being made for taking the water out at the present point, and will show also that the same Court who made the order in that case was the Judge who tried the water suit and entered the decree in case 1953.

The COURT: It seems to be a far fetched defense but the Court will allow it to be introduced and if not material it will be ignored.

Mr. WILSON: Exception.

Thereupon Exhibit 14 was admitted in evidence and is as follows: [249]

EXHIBIT NO. 14.

In the Fourth Judicial District Court.

State of Montana,
County of Missoula.—ss.

Missoula Water Company, a Corporation,
Plaintiff,

vs.

J. S. Kemp,

Defendant.

Plaintiff complains of the defendant and for cause of action alleges:

That the plaintiff is and at all the times hereinafter mentioned was a corporation organized and existing under the laws of the State of Oregon.

That the said plaintiff was organized for and for several years last past has been engaged in the business of supplying the City of Missoula and the residents thereof and in the vicinity thereof with water for domestic, agriculture, fire and other useful and beneficial purposes.

That the defendant is the owner of the southwest quarter of the northeast quarter and the northwest quarter of the southeast quarter of S. 2 T. 10 N. R. 19 W.

That the increased consumption of water and the prospect of increase in the requirements for water by the City and residents of the City of Missoula and vicinity for the purposes aforesaid and to obtain a supply of water pure and unpolluted and free from deleterious substances it has become necessary for the said plaintiff to lay, construct and maintain a new or other flume or pipe line as a conduit, taking and diverting the water from the Rattlesnake Creek at a point above the present point of diversion and taking it thence to a point higher on the hill or bluff north of the City of Missoula and this is necessary also for the purpose of giving to the City of Missoula, in order to protect it against conflagration and to enable it to successfully fight fires, and additional pressure.

That in order to divert said water and to make the improvement necessary and required it is and

has become necessary to construct on the land of the defendant a dam or weir for the purpose of raising the said water and also for right of way for said main, pipe line or conduit across the land of the said defendant, said right of way being for a pipe line laid under ground across said land.

That in the construction, operation and maintenance of the said weir, dam, flume, or pipe line a small portion of the land of the said defendant will be flooded or overflowed. [250]

That a particular description of that portion of the said defendant's land required for the purpose of the said weir or dam site and for flowage hereinabove enumerated is described as follows, to-wit: Beginning at a point 2100 feet west, and north $3^{\circ} 5'$ east 124.6 feet from the quarter corner between sections 1 and 2, T. 13 N. R. 19 W. of the P. M. M., thence north $3^{\circ} 5'$ east 102.6 feet; thence north $19^{\circ} 9'$ East 104.6 feet; thence $8^{\circ} 49'$ east 432.5 feet; thence North $37^{\circ} 23'$ West 165 feet; thence north $81^{\circ} 51'$ west 60 feet; thence south $25^{\circ} 24'$ west 330 feet; thence south $16^{\circ} 10'$ west 400 feet; thence south $74^{\circ} 15'$ east 313 feet to place of beginning, containing an area of 4.28 acres. That a map or plat of said land is herein filed as part hereof marked Exhibit "A".

That portion required for right of way for said flume or pipe line leading the water from said weir or dam is described as being fifteen (15) feet on either side of a center line, described as follows, to-wit: Beginning at a point 772 feet south from the center of S. 2 T. 13 N. R. 19 W. P. M. M.; thence

north $35^{\circ} 20'$ east 38 feet; thence on a curve of 20° to the left 95 feet; thence north $16^{\circ} 20'$ east 264.2 feet; thence on a curve of 30° to the left 90 feet; thence north $10^{\circ} 40'$ west 61.9 feet; thence on a curve of 36° to the right 107.9 feet; thence north $28^{\circ} 10'$ east 461.4 feet; thence north $61^{\circ} 45'$ east 29 feet, making a total distance of 1147.4 feet and 30 feet in width, being 15 feet on either side of the center line, containing an area of 80/100 acres. That a map or plat showing the said land and right of way is herein filed as part hereof, marked Exhibit "B".

That the said plaintiff has made an effort and endeavored to arrange with the said defendant for the purchase of said easement for said weir, dam, flowage right and right of way, but that the said plaintiff and defendant have been unable to agree with respect thereto, and that the plaintiff is ready and willing and hereby offers to pay to the said defendant the reasonable value of the lands required as aforesaid and the damages resulting to the said defendant by reason thereof, but that he cannot arrange to purchase the said right required as herein set forth.

WHEREFORE Plaintiff prays a judgment against said defendant and decree of this court that the easement over, across and upon the land of the said defendant for the construction, maintenance and operation of said weir, dam, flume or pipe line be condemned and that said plaintiff have and recover the easement for said purpose and to the

end that the said plaintiff may make compensation to the said defendant therefor, plaintiff prays that this court will appoint three disinterested persons, residents of the County of Missoula, to view, appraise and value to the value of the lands of the said defendant so taken and required as aforesaid, together with any and all damages that may be sustained by him and that the said plaintiff have such relief in the premises as the situation seems to demand and as in duly bound will ever pray.

S. G. MURRAY &
MARSHALL & STIFF

Attorneys for Plaintiff. [251]

State of Montana,
County of Missoula—ss.

Fred T. Sterling being duly sworn on his oath deposes and says that the plaintiff in the foregoing action is a corporation organized and existing under the laws of the State of Oregon; that he is the agent and attorney in fact of the said plaintiff; that he has heard read the foregoing complaint and knows the contents thereof and that the same is true to his best knowledge, information and belief.

FRED T. STERLING.

Subscribed and sworn to before me this the 17th day of June 1901.

[Seal]

HENRY C. STIFF,
Notary Public in and for Missoula
County, Montana.

Following indorsement on back:

No. 1930. In the District Court of the Fourth Judicial District of the State of Montana, in and for Missoula County. Missoula Water Co. Plaintiff, vs. J. S. Kemp, defendant. Complaint. Filed 17 day of June 1901, R. W. Kemp, Clerk, by J. S. Kemp, Deputy Clerk. S. G. Murray, Marshall & Stiff, Missoula, Montana, Attorneys for Plaintiff.

Office of the Clerk of the District Court of the Fourth Judicial District of the State of Montana, in and for the County of Missoula—ss.

I, J. R. Donehoo, Clerk of the Fourth Judicial District Court of the State of Montana, in and for the County of Missoula, said Court being a Court of Record, having a common law jurisdiction, and a Clerk and Seal, do certify that the above is a true copy of the complaint in Cause No. 1930, as the same appears upon the Records of said Court, now in my office.

IN TESTIMONY WHEREOF, I have hereunto set my hand and affixed the Seal of the said Court at Missoula, Montana, this 26th day of October, in the year of our Lord, one thousand nine hundred and Thirty Three.

J. R. DONEHOO,
Clerk. [252]

Thereupon Exhibit 15 was offered and admitted in evidence over plaintiffs' objection and is as follows: [253]

EXHIBIT NO. 15.

In the Fourth Judicial District Court

State of Montana,
County of Missoula.

Missoula Water Company,

Plaintiff,

vs.

James S. Kemp,

Defendant.

This cause coming on to be heard this the 10th day of August, 1901, upon the order to the said defendant contained in the summons to show cause, if any he had, why the property mentioned in the complaint should not be condemned for right of way of weir, dam and pipe line for plaintiff's water works, and commissioners appointed to appraise the damage by him sustained by reason of the appropriation of said property for the purpose aforesaid, and the same having been heard by the court on the 3rd day of August and by it taken under advisement.

And it appearing to the Court that the said James S. Kemp had appeared in said action and filed a demurrer to the complaint, S. G. Murray and Marshall & Stiff appearing for the plaintiff and Woody & Woody appearing for the above named defendant and demurred to the said complaint.

NOW, THEREFORE, the said demurrer is hereby overruled and the Judge of this Court being satisfied that the public interests require the prosecution of the enterprise mentioned in the complaint and that the lands proposed to be taken are required and necessary for the purpose of said enterprise.

NOW, THEREFORE, John Rankin and O. E. Peppard and George F. Brooks, three competent and disinterested persons, citizens of the said County of Missoula, be and they are hereby appointed commissioners to ascertain and determine the amount to be paid by the plaintiff to the said James S. Kemp as compensation for the land taken and other damages by reason of the appropriation of said property by the plaintiff. It is further ordered that the said commissioners hold their first meeting at the office of the Clerk of this Court in the City of Missoula, County of Missoula, Montana, on the 20th day of August, 1901, at two (2) o'clock P. M. and that the compensation of the said commissioners be and the same is hereby fixed at the sum of ten dollars each, for each and every day by them actually and necessarily employed in and about the duties as such commissioners.

And the said commissioners shall within thirty (30) days after making their appraisement and assessment of damages file a report of their proceedings accompanied by a map of the dam site and right of way showing the location and termini thereof. Done in open court this 10th day of August, 1901.

FREDERICK C. WEBSTER,

Judge. [254]

Following indorsement on back:

1930/4

Missoula Water Co. vs. James S. Kemp.

Order appointing Commissioners. Filed August
10th, 1901.

R. M. Kemp, Clerk H 128

Office of the Clerk of the District Court of the
Fourth Judicial District of the State of Mon-
tana, in and for the County of Missoula—ss.

I, J. R. Donehoo, Clerk of the Fourth Judicial
District of the State of Montana, in and for the
County of Missoula, said Court being a Court of
Record, having a common law jurisdiction, and a
Clerk and Seal, do certify that the above is a true
copy of Order Appointing Commissioners, No. 1930,
Missoula Water Co. vs. James S. Kemp, as the same
appears upon the records of said Court, now in my
office.

IN TESTIMONY WHEREOF, I have hereunto
set my hand and affixed the Seal of said Court at
Missoula, Montana, this 26th day of October, in the
year of our Lord, One thousand nine hundred and
Thirty Three.

J. R. DONEHOO,

Clerk. [255]

Mr. WHITLOCK: And counsel have agreed
with me, and the record may show, that the Judge
who signed the order, being the last exhibit intro-

duced, was Frederick C. Webster, the same Judge who tried and signed the decree in cause number 1953, and that J. S. Kemp, the defendant in the action, the complaint in which has just been introduced, was likewise a defendant in cause number 1953.

Mr. WILSON: We agree to that, subject to our objection that it is incompetent.

The COURT: Very well. Overruled.

Mr. MURPHY: There was no transcript of the evidence at all in the cause 1953,—I desire to correct that statement by saying that there was a transcript prepared on one right, the Williams right, which I have seen.

The COURT: Very well.

Mr. WHITLOCK: Defendant rests.

PLAINTIFFS' REBUTTAL

WILLIAM SWEARINGEN,

called as a witness in rebuttal and having been heretofore sworn testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

I have heard the witnesses mention the tube or pipe crossing the road on the Fredline ditch and carrying the water flowing in the Fredline ditch on down. I have measured the carrying capacity of that pipe yesterday, which carrying capacity is between 160 and 250 miners inches. The ditch itself will carry

(Testimony of William Swearingen.)

more water than the pipe will, because the city has had trouble with it in several years past by overflowing [256] at Van Buren Street, where it crosses Van Buren Street, because the pipe does not have the capacity to carry the water coming to it across the street. The carrying capacity of the ditch is greater than that of the pipe.

I heard Mr. Hagens' testimony given yesterday to the effect that water used upon the lands in Rattlesnake Valley east of the creek for irrigation, instead of seeping and percolating under ground, took back westwards and southwestwards and into Hellgate River, and I have had occasion to make observations reflecting on that condition in this way: That I was on the original sewer job proposed from the Rattlesnake creek, with my father; since then I have refreshed my memory from these notes. There is what is known as a rock dyke running in a southeasterly or northwesterly direction across the Rattlesnake Valley pretty generally from the lower end of the Greenough Park over towards the mouth of Hellgate canyon, and that dyke naturally would force any water coming down through there to come to the surface or very close to the surface at that point. This Greenough Park wouldn't be over 600 feet north of the head of Mill ditch, that is, the south end of Greenough Park would be 300 to 600 feet north of the intake into the Mill ditch. From that point Greenough Park extends approximately a quarter of a mile north of the city limits. This rock

(Testimony of William Swearingen.)

dyke or rock formation would cut the Rattlesnake Valley, and running eastwards. The rock formation in all this country slopes more or less southwesterly, that is, the stratafication runs down towards the south and west, and that applies to the east side of the Rattlesnake Valley or Rattlesnake Creek.

CROSS EXAMINATION by Mr. Whitlock:

The first evidences of this dyke is about 100 feet [257] north of the south end of Greenough Park and three and a half miles below defendant's dam. The direction of the dyke is toward the Missoula River, more toward what we call the foot of Jumbo, east of the Rattlesnake.

RUSSELL MILLER,

called as a witness in rebuttal and having been heretofore sworn testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My explanation of why I did not bring nor participate in bringing a suit such as this previously to the year 1933 is that if the Water Company or anyone had taken all my water I most certainly would have gotten down to business. As it was, at times the Water Company took a part of it, that is, in the dry season. Now the amount they took to the portion of the whole amount would be almost negligible, maybe one-half of one percent, if you consider the whole flow of my water for the year. And then here

(Testimony of Russell Miller.)

was another thing. When I went there, or after being there for a while I had confidence enough in my water flow, being there with it for several years, that I borrowed money and put in a young cherry orchard and I have grown that cherry orchard over a period of eight or ten years into maturity and it was in maximum production. If I had been lax about looking after my water I wouldn't have grown my cherry orchard to that extent, and I didn't consider that because of the times I lost a small portion of my water that meant that I had neglected my water rights as a whole, when the Hamilton ditch immediately above, maybe twenty rods above the Hollenbeck ditch, practically every year for short periods has thrown a dam across and taken all of the water maybe three or four days before we realized what had happened, and we would go and see about our water. Well now they would have our water [258] for short periods, but that wouldn't necessarily mean I figured they had a right to our water because they took it up there, and for that matter when the Water Company would,—or sometimes I figured the Water Company wouldn't come down the creek,—anyway it wasn't for me,—when the Hollenbeck ditch got short and I didn't get enough water I used to go up the creek where the ditch,—where they had water for me higher up, and turn on a big head of water in that ditch and carry it down across my land to the Hollenbeck ditch and water my stock anyhow. Now I presume at times I was taking maybe the city

(Testimony of Russell Miller.)

maybe Lord knows whose water it was, water above the dam; they had taken my water below and I was right if I took it above and carried it across my land to the Hollenbeck ditch, and I figured not because I wouldn't have the nerve to presume that because the Water Company had,—because I had had the Water Company's water in those periods that they had lost any rights to it; that has been my theory of it; there hasn't been the urge to go ahead and carry on a suit as long as I didn't have enough provocation, I would get my crop and I developed my orchard and things have been fairly satisfactory. I do say this, I believe they have got more of my water at any rate than I have theirs.

Concerning the slope, I have made observations of the slope on both sides. We have two or three levels; we call them benches. Each bench is a drop of 8 or 10 feet from the one above. Practically all the land irrigated is on the upper bench and the slope is generally toward the Rattlesnake, although of course, it also slopes towards the river.

J. C. SAIN,

one of the plaintiffs, was called in rebuttal, and testified as follows: [259]

DIRECT EXAMINATION by Mr. Wilson:

The reason I haven't started nor joined in the bringing of a suit such as this previously to the

(Testimony of J. C. Sain.)

year 1933 is because in 1925, which was a dry year, they, the Water Company, were taking practically all the water, so in 1926, we made our weir and we checked up on them, and they were taking our water. The dam and works of defendant's predecessor were built long prior to the year 1925 and the pipeline was constructed and installed before 1925, also the reservoir; previous to that time I had been able to get my water and grow my crops and work my land reasonably well. As to the slope or drainage of water used for irrigation on the east side of Rattlesnake creek in Rattlesnake valley, on my place, I got a bench above where I grow alfalfa, and a bench a little lower down, and I got to be very careful watering this alfalfa or I drown out this bench below. The bench below lays on the west side of the alfalfa field and next to the Rattlesnake towards Rattlesnake creek. I only irrigated that place once this summer. That was along about the last of July—when the water began to get a little scarce I could water the alfalfa, it never got dry. When I watered the alfalfa there was moisture on this lower bench.

CROSS EXAMINATION by Mr. Whitlock:

I have no knowledge of water being taken into the Mill ditch since I have been farming on Rattlesnake.

I. Q. ROBERTS,

called in rebuttal and testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

I located up Rattlesnake in the spring of 1902 and the reason I did not bring nor participate in bringing a suit such as this previous to 1933, is because I've got only a very small [260] tract of land, only five acres, and I have a right in two ditches and I used to have sufficient water to raise my crops, I had no reason to make any complaint. I get a right out of No. 5 through the Williams ditch which takes out above defendant's dam, and the rest of my water takes out through the Cobban-Raymond ditch below the dam.

ED RAY,

called as a witness in rebuttal, having been heretofore duly sworn testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My water right is taken out through the Effinger ditch above the dam.

The reason I did not bring nor participate in bringing a suit such as this prior to 1933 is that in 1921, 1922, and 1923 I had the water just the way it was decreed, and then in 1924 they started to take all,—well they took it maybe in the day time and nights they let me have it and then I opened up the ditch and had it again and flooded my land;

(Testimony of Ed Ray.)

they never took it away from me until in later years. In 1929 they took it and in 1926. I remember 1931; they took it that year, but I went up and got it.

CROSS EXAMINATION by Mr. Pope:

We had rows in 1924 over the water. There was no water commissioner that year and the Water Company shut down my ditch and I know they had no right, and we had rows back and forth. I told them once that he better leave my headgate alone, and he did. I testified yesterday that in 1924 I went to see my attorney about it.

L. E. TUCKER,

called as a witness in rebuttal and testified as follows: [261]

DIRECT EXAMINATION by Mr. Wilson:

While living in Rattlesnake Valley I have made observations as to the drainage of water used in irrigation. It drains southwesterly, considerably more west than south. Mr. Miller's place was just below me, pretty near west of where I had irrigated and he used to complain considerably to me when I would be irrigating, about my drowning his crop out below. His land was toward Rattlesnake Creek from mine. I judge, his land was a quarter of a mile from the Rattlesnake Creek channel.

(Testimony of L. E. Tucker.)

I had 45 inches from right No. 5, taken through the Williams ditch above defendant's dam. I had 40 inches in the Hollenbeck ditch coming out below the dam. Right #20 was taken out through the Quast-Kemp ditch or Quast-Tucker ditch, which takes out above the dam, probably between a quarter and a half mile. Right No. 21 takes out through the Cobban-Raymond ditch, which heads below the dam. The year 1926 was a fairly representative year, average year, of the flow of Rattlesnake Creek from a seasonal standpoint, a water standpoint. I think there was a little more water in 1927 and in 1925, but 1926 was a fairly average year.

CROSS EXAMINATION by Mr. Whitlock:

I am speaking for the time I lived on Rattlesnake.

It was agreed between counsel, while the witness Tucker was testifying that the ditches shown upon the maps and mentioned at the trial constitute all the ditches that take water out of Rattlesnake Creek.

J. S. JACKMAN,

called as a witness in rebuttal and having been first duly sworn, testified as follows:

DIRECT EXAMINATION by Mr. Wilson: [262]

I reside in Rattlesnake Valley up on the bench a quarter of a mile east, about a mile above Greenough Park; and have made observations as to the drainage in Rattlesnake Basin of water used for

(Testimony of J. S. Jackman.)

irrigation on the bench on the east side. When irrigation is a heavy flow in the valley, seepage water rises up in our cellar every year; we have a concrete cellar, made nearly water tight, and yet water comes up after the crest of the high water in the creek. This year the first water appeared in our cellar on July 5th; high water in the creek was then past; the maximum rising in the cellar was July 7th and remained thirty days. This cellar is approximately a quarter of a mile from Rattlesnake Creek and about a mile above the head of the ditch.

CROSS EXAMINATION by Mr. Pope:

The irrigation on Rattlesnake is practically all north above my place.

REDIRECT EXAMINATION by Mr. Wilson:

The surface flow at my place, to show whether the drainage is southwestwards to the Missoula River or westwards to Rattlesnake Creek, I explained directly east of our concrete cellar, we have an open pit; it is about two or three feet deeper than the water, and my observation is that the rise and fall in the water in these two places is simultaneous. The irrigation, with reference to my place, is north, slightly eastward, about 10° east. I live on the Jackman Floral Villa, and I would say from my place the water will flow more toward Rattlesnake Creek than toward the river.

RECROSS EXAMINATION by Mr. Pope:

Witness places cross mark on map, Plaintiffs' Exhibit 1, with pencil, just below where words

“Park Addition” are written, [263] as the location of his place.

JOE McDONALD,

called as a witness in rebuttal and testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

My observations as to draingage of water used for irrigation on the east side of Rattlesnake Creek in Rattlesnake Valley is that it is all practically to the west, with a little south. I have made observations as to that. On the same bench as Mr. Miller described, when I am irrigating a little north of Mr. Miller's place, the water will rise on the lower land by the barn and one place a regular spring. I have alfalfa that is drowned out, which is directly west of where I have irrigated, and toward Rattlesnake Creek. The first year I worked the land I occupy was 1931.

I got plenty of water that year to the middle of July, when right No. 20, where I got the bulk of my water was shut down completely and kept down for three weeks and my crop completely burned up; by that I mean it was completely lost. In one field I didn't even get pasture. I had a little more water in the beginning of 1932 and got a crop in a little early with this early runoff water, but was shut off completely in the first part of August and was caused considerable damage before the crop

(Testimony of Joe McDonald.)

was matured. I used the same system in 1933 and got the crop in early and with an early variety of grain, which matured before the water was shut off, which wasn't until later in August.

CROSS EXAMINATION by Mr. Wilson:

My west boundary is in places an eighth of a mile and some places a half mile from Rattlesnake Creek, and my east boundary is some two miles up in the hills. My buildings are less than a quarter of a mile from the creek. The upper ditch crosses [264] the full length of my place for some two miles from where it enters, and it enters on the northwest corner, 100 yards from the creek and leaves it about a half mile from the creek.

C. W. LEAPHART,

called as a witness in rebuttal and testified as follows:

DIRECT EXAMINATION by Mr. Wilson:

I have made observations as to the drainage on the east side of Rattlesnake Creek in Rattlesnake Valley. My observations were largely in connection with the Hollenbeck ditch, the ground above that is always seepage from the irrigation on Mr. Sain's place, and that seepage water is coming pretty well down west. Mr. Martinson has an ice pond and complains when we are irrigating that we are flooding his place and although we are careful, there

(Testimony of C. W. Leaphart.)

has always been a heavy seepage down into his ice pond, which is going west from our ditch, and he wants to keep free of water during the summer time. Another seepage we notice especially is in connection with this Fredline ditch. When the water gets short, we block all the water coming down the Rattlesnake at our dam at the head of Hollenbeck creek. The water commissioner insists even before the water is at its shortest point that we place sacks across the creek in order to get all the water that is coming down so that none will go to waste, so that our dam turns the entire flow coming down the creek into the Hollenbeck ditch, and we have also dammed off the west branch of the creek, because our Hollenbeck ditch is superior to the Hammond-Day-Brennan ditch. We have a concrete dam and have sacked to make a complete dam across the stream, and fill in with loose dirt in every way we can, thus taking the entire flow of Rattlesnake Creek at that point. Sometimes we get more than our 195 inches decreed for the ditch and that [265] has been our practice since prior to the year 1924, the water commissioner insisting that we do not permit any waste water to run past our dam.

The reason that I did not bring or participate in bringing an action such as this prior to 1933 was because the Hollenbeck ditch is fairly fortunately situated in that the ditch gets a seepage of about 40 inches, between the dam and the head of Hollenbeck ditch; then we get the morning spill from the

(Testimony of C. W. Leaphart.)

dam, and that helps somewhat, and while I have been irritated with the shortage a little in previous years I have never failed to have my land in growing condition. It never dried up.

Adding to what I have said about seepage water, we live north of Roscoe Jackman's place and we who live east, it takes two jogs in the road of about 100 yards each before we strike that south line going by the Jackman place and that is out of my south line. Now there are other farmers, Mr. Sain and a small place west of me and one or two others that are doing irrigating to the west of us but most of this irrigating is still to the east of my west lines.

CROSS EXAMINATION by Mr. Whitlock:

The Hollenbeck ditch has been cleaned out either last year or the year before, 1931 or 1932. Before that it had a concrete dam and now a concrete dam which is a little on the west side for high water time and the space is filled up with sacks. We dam it full with sacks of dirt and earth all the way across. Those are placed on the surface. I suppose at the driest time there is water going to the west of that dam. The branch to the west is called the Hamilton-Day-Brennan ditch. It runs a little west then the ditch takes it all. The Hollen- [266] beck ditch always gets some seepage, which I estimate at around 40 inches. The course of the ditch is generally southeasterly from the creek.

(Testimony of C. W. Leaphart.)

EXAMINATION by the Court:

Q. Seepage from where?

A. Seepage from,—you mean into the Hollenbeck ditch?

Q. Yes.

A. I have never examined it closely from there on above; I know that when the dam was cut to enter that we still have that water in the Hollenbeck ditch when no water is going over the dam, there is still water coming in the Hollenbeck ditch.

Q. You mean it comes out of the creek?

A. Yes it comes out of the creek.

Q. You mean that the seepage is down the creek, from the creek bed?

A. It comes from the creek bed where it seeps in.

Q. The Court understood you to say you got along reasonably well?

A. I have gotten along reasonably well.

Q. How many use water and drown out the neighbors?

A. No one, I don't think that there has been a remonstrance of anyone drowning out the neighbors; now I spoke yesterday about this drowning out of Mr. Boles potato patch a little further down.

Q. Well you speak here of from Sain's place there is some seepage down below?

A. Yes that is all, it is pasture ground, from the Hollenbeck ditch, it is still his ground but it is pasture land and it is a wet field during the dry time of the year.

(Testimony of C. W. Leaphart.)

Q. In other words you say in your ditch there is not much [267] wastage from it, continuing to the ice pond?

A. I don't think it comes from our ditch, no, it is coming out,—of course that is Mr. Martinson's claim and I don't know, I suppose maybe some of it comes from our ditch, as careful as we may try to be,—but it is coming out of the hillside or seepage that comes from the bed of the stream. There is one thing I might mention that I think Mr. Jackman covered, that our water there frequently will vary so that the well goes dry, and then the Rattlesnake,—it goes dry around February; the rise in the water will be,—my well is 52 feet deep; I have had occasion to put an electric pump on it and I have to have it set in the well pretty well up in the winter time. I have maybe two or three feet of water all the time; in the summer time it will be within 17 feet of the surface and at the time that is high irrigation is the lowest time in the well, which I suppose is natural.

CROSS EXAMINATION (continued)

by Mr. Whitlock:

It is 300 or 400 yards from my well to the creek channel. My land is on the benches and at the foot of Jumbo mountain, and the well is about 125 yards or 150 yards from the foot of the mountain.

Mr. WILSON: I am going to offer in evidence a certified copy of the judgment roll of the district Court of Missoula County in cause 9658, in the case

(Testimony of C. W. Leaphart.)

in which L. E. Tucker was plaintiff and Missoula Light and Water Company, a corporation, and C. H. Christensen, was defendant. This Missoula Light and Water Company was the predecessor of defendant.

Mr. WHITLOCK: Objected to as not material to any issue [268]

The COURT: What is the object?

Mr. WILSON: It is offered on the question of laches of the predecessor of the plaintiff McDonald, and it shows the taking of the water by the defendant company, and we think possibly of the present defendant, during the years involved in this action, which were the years 1921, 1922 and 1923, was over the protest of the then occupant and owner of the lands, and for which he sued for damages and which judgment for damages was given him and which was paid by the Missoula Light and Water Company for the taking of this water from him.

Mr. WHITLOCK: We further object to it——

The COURT: ——It will be admitted; if not competent the Court will ignore it.

Mr. WHITLOCK: Exception.

Thereupon was received in evidence the instrument referred to which is identified as Plaintiff's Exhibit 16, on file with and a part of the original exhibits in this cause.

The judgment roll here offered in evidence and being plaintiffs' Exhibit 16 is lengthy and for brevity the same is not here set forth at length but is in substance as follows: The plaintiff who was the predecessor in interest of Joseph H. McDonald, one of the plaintiffs in this action in the ownership of the lands and water rights claimed by said Joseph H. McDonald, brought suit to recover damages against the defendant who was the predecessor of the defendant in this action and a public service corporation supplying Missoula and its inhabitants with water from Rattlesnake Creek; plaintiff in that action claiming that during the irrigation seasons of 1922, 1923 and 1924, the defendant in that action diverted and used the waters of Rattlesnake Creek which said plaintiff was entitled to use. Plaintiffs' [269] use was for irrigation upon his lands consisting of One Thousand Three Hundred Fifty-six (1,356) acres of which One Hundred Seventy-five (175) acres were irrigable from the waters of Rattlesnake Creek and from no other source. The complaint refers to and describes in haec verba the decree in cause No. 1953, and is in three counts, the first for alleged, unlawful interference in 1922 with plaintiffs' use of the water, the second for alleged, unlawful interference in 1923 with plaintiffs' use of the water, and the third alleged, unlawful interference during 1924, with plaintiffs' use of the water. Except as the same apply to different years, the character of the claims in the several causes of action are the same. The plaintiff claimed damages totaling upon the three

causes of action the sum of \$46,403.00. By answer plaintiffs' claims for damages were denied and certain affirmative matters, not herein important, were set out which were put in issue by a reply. Before trial was had with a jury and by the pleadings and the stipulations of the parties, the trial resolved itself concisely to the question of defendant having prevented plaintiff using water which plaintiff had the right to use for the irrigation of his land and the extent of the damage done by such interference, if interference there was. The jury returned a verdict for the plaintiff for \$22,726.90 and judgment thereon is as follows:

JUDGMENT ON VERDICT.

This action came on regularly for trial upon the 28th. day of January, 1926, the said parties appeared by their Attorneys S. P. Wilson and Mulroney & Mulroney, Counsel for plaintiff, and Fred J. Furman and W. M. Bickford, Counsel for Defendants. A jury of Twelve persons was regularly impanelled and sworn to try said cause. Witnesses on the part of the plaintiff were sworn and examined. No witnesses were sworn or examined on behalf of the defendants, or either of them. [270]

After hearing the evidence, the arguments of Counsel and instructions of the Court, the Jury retired to consider of their verdict, and subsequently returned into Court with the following verdict, which was duly received and filed, to-wit: Title of Court. "L. E. Tucker, Plaintiff, vs. Missoula Light and

Water Company, a Corporation, and C. H. Christensen, and Missoula Public Service Company, Successor to Missoula Light and Water Company, defendants.

VERDICT.

We, the jury in the above entitled action, find the issues herein in favor of the plaintiff and against the defendant, and we fix the plaintiff's damages at the sum of Twenty-two Thousand seven hundred and twenty-six Dollars and 90 cents, \$22726.90, together with interest at the rate of 8%.

G. E. WARD, Foreman."

Wherefore by virtue of the law and by reason of the premises aforesaid, it is ordered, adjudged and decreed that the plaintiff, L. E. Tucker, do have and recover judgment against the defendants Missoula Light and Water Company, a corporation, and C. H. Christensen, and Missoula Public Service Company, Successor to Missoula Light and Water Company, for the sum of Twenty-two thousand seven hundred and twenty-six dollars and ninety cents (\$22726.90), together with his costs herein fixed at the sum of \$177.90.

Judgment entered this 4th day of February, A. D. 1926.

[Seal]

H. M. RAWN, Clerk.

RUTH KEITH, Deputy Clerk.

An appeal was taken by defendant and was decided and is reported in *Tucker vs. Missoula Light and Railway Company et al.*, 77 Mont. 91 and 250 Pac. 11.

E. C. MULRONEY,

called as a witness in rebuttal and having been first duly sworn testified as follows:

DIRECT EXAMINATION by Mr. Wilson: [271]

The judgment, entered in the case in which the judgment roll has just been introduced was finally paid by the defendant after the judgment had been affirmed by the Supreme Court.

Mr. WHITLOCK: Counsel called my attention that perhaps the exact difference in elevation between the old mill ditch and the defendant's dam does not appear, in [272] feet. Counsel have agreed with us to take the engineer's figures for that. The difference in elevation is 305 feet.

Counsel have agreed that the old reservoir on the top of the hill above Missoula was close to the present reservoir on top of the same hill.

Mr. MULRONEY: Yes, we agree to that.

And thereupon the testimony was closed.

Mr. WHITLOCK: If that is all of the evidence the defendant, for the purpose of the record, at this time after the close of all of the evidence moves to dismiss this action for the reasons:

First: That there are no facts shown here entitling the plaintiffs to any equitable relief.

Second: That there is no evidence of any detriment caused to the plaintiffs by the diversion of water by the defendant at the present point of diversion and no evidence even bearing on that ques-

tion related to the time when the plaintiff's appropriations were made or when the point of diversion was first established at the present point.

Third: For the reason that the diversion of the water at that point, as shown by the uncontradicted evidence, has been continuous and uninterrupted under claim of right for more than thirty years.

Fourth: For the reason that the evidence does not show the defendant has at any time deprived the plaintiffs or any of them of any water [273] to which they or he were entitled.

And for the further reason that under the evidence shown here the plaintiffs are barred from maintaining any action by virtue of their laches in the premises.

Thereupon the case was by the Court taken under advisement, with the understanding that the matter should be submitted on briefs.

Mr. WHITLOCK: If the matter is to be submitted on briefs we would like a ruling upon our motion to dismiss.

The COURT: That will be taken under advisement along with the case itself.

Mr. WILSON: Plaintiffs would like to make request for findings for the Court to make findings of fact in the case, and the plaintiff would like the privilege of submitting their request for findings with the brief.

The COURT: You may.

Mr. WHITLOCK: And the defendant joins in the request that the Court make findings of fact and

conclusions of law, and now at the close of the evidence submits and asks leave to file their proposed findings of fact and conclusions of law in this action.

The COURT: It may be done.

Thereupon plaintiffs were allowed ten days within which to file proposed findings of fact and conclusions of law and the defendant was given ten days thereafter within which to file proposed findings of fact and conclusions of law.

Plaintiffs' request for findings are as follows:
[274]

FINDINGS OF FACT AND CONCLUSIONS OF LAW

FINDINGS OF FACT

I.

Plaintiffs are and each of them is a citizen of the State of Montana, and a resident of Missoula, Montana; defendant is a corporation organized and existing under the laws of the State of New Jersey and is a citizen of the State of New Jersey. Jurisdiction in this case arises and is conferred upon this court by reason of the diversity of citizenship of the parties to the action. The matter in controversy in the action, exclusive of interest and costs, exceeds the sum and value of \$3,000.00.

II.

That Missoula County, one of the plaintiffs herein, is a body politic and corporate, organized and existing under the laws of the State of Montana; that

Missoula Ice Company, one of the plaintiffs herein, is a corporation, organized and existing under the laws of the State of Montana; that Montana Power Company, the defendant herein, is a corporation organized and existing under the laws of the State of New Jersey.

III.

That Rattlesnake Creek, described in this complaint, is a stream of fresh and flowing water arising in the mountains north of Missoula in Missoula County, Montana, and flowing southwardly into Missoula River and is a tributary of said Missoula River and is situated in Missoula County, Montana.

IV.

That upon the 9th day of July, 1930, in the District Court of the Fourth Judicial District of the State of Mon- [275] tana, in and for the County of Missoula, in a cause then pending in said Court, wherein the Missoula Water Company was plaintiff and Charles E. Williams and others were defendants, being Cause No. 1953 of said court, a decree was duly given, made, rendered and entered, adjudicating the waters of said Rattlesnake Creek between appropriators and claimants to the use of the waters of said creek and determining the respective rights, priorities and amounts to the use of such waters among the said appropriators and users thereof, a copy of said decree and judgment is attached to and made a part of the complaint

herein and is hereby referred to. By the judgment and decree aforesaid the rights, priorities, amounts of water and dates of appropriations of the waters of Rattlesnake Creek were fully adjudicated and determined and said Rattlesnake Creek became, and thereafter was, an adjudicated stream, as defined by Section 7128, Revised Codes of Montana, 1921, and that said judgment has not been reversed nor in any way modified nor set aside.

V.

That in said Cause No. 1953 the Court did make findings of fact, Finding of Fact No. 1 being as follows:

“1. That the plaintiff by its predecessors in interest made an appropriation of 946 inches of waters of Rattlesnake Creek, mentioned and described in the complaint herein, about April 1, 1866, by what is called the Mill ditch, for mechanical, power and other beneficial purposes, and that the same has been used by plaintiff and its predecessors in interest ever since, and that no part thereof has ever been abandoned.”

Findings of Fact No. 2 being:

“2. That the plaintiff by its predecessors in interest made an appropriation of 160 inches of the waters of said Rattlesnake [276] Creek November 16, 1868, by what is called the original Higgins ditch, and that no part of said appropriation has ever been abandoned.”

Findings of Fact No. 9 being:

“9. That the plaintiff, by its predecessors in interest, about May 1, 1881, enlarged the original Higgins ditch and extended it to other lands, increasing its capacity and use from 160 inches to 508 inches, thereby making an additional appropriation of the waters of said Rattlesnake Creek of 348 inches, of date May 1, 1881, and that no part thereof has ever been abandoned.”

Defendant claims ownership of the water rights and appropriations of the waters of Rattlesnake Creek found, decreed and described in said Findings of Fact 1, 2 and 9, foregoing described, and defendant at the times alleged in the complaint in this action has assumed possession of said water rights and appropriations of water and has diverted said water from said Rattlesnake Creek and has made use thereof and claims the same.

VI.

That the water right and appropriation of water described in Finding of Fact No. 1, foregoing, was appropriated through what is called the Mill ditch out of said Rattlesnake Creek and at all times from the time of the appropriation thereof down to and subsequent to the date of the judgment in said Cause No. 1953, said water so appropriated and found and decreed in said Cause No. 1953, was diverted out of Rattlesnake Creek through said Mill ditch and was used for mechanical and power purposes along said Mill ditch.

That the water right and appropriation of water described in Finding of Fact No. 2, foregoing, was appropriated through what is called the original Higgins Ditch out of said Rattlesnake Creek and at all times from the time of the appropriation thereof down to and subsequent to the date of the judgment [277] in said Cause No. 1953, said water so appropriated and found and decreed in said Cause No. 1953, was diverted out of Rattlesnake Creek through said original Higgins ditch and was used for irrigation upon agricultural lands along said original Higgins ditch.

That the water right and appropriation of water described in Finding of Fact No. 9, foregoing, was appropriated through what is called the original Higgins ditch enlarged out of said Rattlesnake Creek and at all times from the time of the appropriation thereof down to and subsequent to the date of the judgment in said Cause No. 1953, said water so appropriated and found and decreed in said Cause No. 1953, was diverted out of Rattlesnake Creek through said original Higgins ditch enlarged and was used for irrigation upon agricultural lands along said original Higgins ditch enlarged.

Said Mill ditch taps said Rattlesnake Creek upon its right bank about a quarter of a mile above the mouth of Rattlesnake Creek. Said original Higgins ditch and as enlarged taps said Rattlesnake Creek upon its right bank at a point about two miles above the mouth of Rattlesnake Creek.

VII.

Defendant Montana Power Company is the successor in interest of the Missoula Water Company,

who was the plaintiff in said cause No. 1953, in the ownership of all waters, water rights and appropriations of water decreed to said The Missoula Water Company in Cause No. 1953, and defendant has taken, and now takes, possession of the waters of Rattlesnake Creek as the successor in title and in interest of The Missoula Water Company to the extent of the appropriations found in said Findings of Fact 1, 2 and 9, foregoing described. [278]

VIII.

That subsequent to the date of the decree in said Cause No. 1953, defendant and its grantors and predecessors in interest abandoned said Mill ditch and went upon said Rattlesnake Creek to a point higher up on said creek than the head of said Mill ditch, that is to say, to a point near the North line of Township 13 North, Range 19 West, the point of the present dam, and there diverted from Rattlesnake Creek 946 inches of water, claiming the same as the water right described in said Finding of Fact No. 1. The water right and appropriation of water described in Finding of Fact No. 1 for 946 inches of water was appropriated and was decreed to be taken from the water flowing in said creek at the head of said Mill ditch.

That subsequent to the date of said decree, defendant and its grantors and predecessors in interest abandoned said original Higgins ditch and went upon said Rattlesnake Creek to a point higher up on said creek than the head of said original Higgins ditch, that is to say, to a point near the North line of Township 13 North, Range 19 West, and there diverted from Rattlesnake Creek 160

inches of water, claiming the same as the water right described in said Finding of Fact No. 2. The water right and appropriation of water described in said Finding of Fact No. 2 for 160 inches of water was appropriated and was decreed to be taken from the water flowing in said creek at the head of said original Higgins ditch.

That subsequent to the date of said decree, defendant and its grantors and predecessors in interest abandoned said original Higgins ditch enlarged and went up said Rattlesnake Creek to a point higher up on said creek than the head of [279] said original Higgins ditch enlarged, that is to say, to a point near the North line of Township 13 North, Range 19 West (designated "Dam" on the maps) and there diverted from Rattlesnake Creek 348 inches of water, claiming the same as the water right described in said Finding of Fact No. 9. The water right and appropriation of water described in said Finding of Fact No. 9 for 348 inches of water was appropriated and was decreed to be taken from the water flowing in said creek at the head of said original Higgins ditch enlarged. The new point of diversion whereat defendant and its grantors and predecessors diverted each said 946 inches, said 160 inches and said 348 inches of water, is identical with the place designated upon the maps introduced in evidence as "Dam".

IX.

Each of the plaintiffs severally owns and is possessed of the premises alleged in the complaint to belong to said respective plaintiff. All of said lands are situated along and in the vicinity of Rattlesnake

Creek, but higher up on said creek than the place where with said Mill ditch or said Original Higgins ditch diverted water. The lands of each plaintiff described in the complaint are agricultural in character, but arid and require irrigation for the successful and profitable working thereof and the enjoyment thereof. As an appurtenant to his land described in the complaint, each plaintiff owns and is entitled to the use and possession of the water right out of Rattlesnake Creek claimed by him in the complaint in this action; all of which said water rights were included in the decree in Cause No. 1953 and were adjudicated in that action; plaintiffs own and are entitled to use said water rights severally, but the aggregate of the water rights decreed to plaintiffs in Cause No. 1953 are as follows:

45 inches of Right 5, through Williams Ditch; 145 inches of Right 10, through Hollenbeck Ditch; 50 inches of Right 16, through Hollenbeck Ditch; 100 inches of Right 17, through Effinger Ditch; 50 inches of Right 18, through Neill ditch; 248 inches of Right 20, through Quast Ditch; 129.3 inches of Right 21, through Cobban-Raymond ditch; 55 inches of Right 22, through Hamilton Ditch.

In addition to said rights, plaintiffs Charles A. Martinson and Freda Martinson, co-partners, doing business under the firm name of Missoula Ice Company, own and are entitled to use 150 inches of the water of said creek as of date, August 1st, 1901, which use is limited to ice manufacture purposes

and after the expiration of the irrigation season in each year when water is not required by any agricultural user.

The use of all such waters by plaintiffs is necessary for the respective purposes of each plaintiff and is a beneficial use.

The names of the several ditches referred to in this findings are the names by which said ditches are commonly designated in the neighborhood and the same are shown upon the maps introduced in evidence and are designated respectively by such names. The same divert water from Rattlesnake Creek at points in the vicinity of said "Dam". Said Effinger ditch, Williams ditch and Quast ditch divert water at different points on the stream all near to and short distances above said "Dam". Said Cobban-Raymond ditch, Neill ditch, Hollenbeck ditch and Hamilton ditch divert water at different points on the stream all near to and short distances below said "Dam". The heads of all said ditches, [281] through which plaintiffs divert water, are located on said stream a long distance above the place where original Higgins ditch diverted water from the stream and above the place where the Mill ditch diverted water from the stream.

X.

In normal years at the low water time of the year, namely, the first two weeks of the month of August of each year, there is about 1,600 miner's inches of water flowing in the creek. For many years previous to the commencement of this action at the place on said stream designated on the maps as

“Dam”, by means of a pipe, defendant has diverted water to supply the City of Missoula and its inhabitants. At such times it has been defendant’s practice to so divert the water of said creek that the whole of such flow at the “Dam” is carried into its pipe line, leaving the bed of the creek below its diversion dam, dry or without a substantial flow. Water raises in the bed and channel of the creek below the “Dam” and above the head of original Higgins Ditch and above the head of the Mill ditch to the extent that during such period of low water, there is again naturally flowing in said stream an amount varying from 400 to 800 miner’s inches at the head of the Mill ditch and which could be diverted into the Mill ditch if so desired. Some of this water so raising in the bed of the creek below the “Dam”, raises and is flowing in the creek at the head of the original Higgins Ditch. During the years complained of in the complaint, namely, during 1931, 1932 and 1933, such water so raising in the creek below the “Dam” for the most part has flowed to waste out of the mouth of the creek and was not available to supply the appropriations of any of the plaintiffs. Unless restrain- [282] ed by the court such conditions will continue in the future. During times when water has flowed to waste out of the Rattlesnake Creek, plaintiffs have needed the water for which they had decreed rights and to the extent of such decreed rights, but were unable to obtain water to supply such rights.

XI.

Defendant, claiming to be the owner, claims the perpetual right to change the point of diversion of

said waters so described in Findings of Fact Numbered 1, 2 and 9, of Cause No. 1953, and so decreed to The Missoula Water Company, to a point near the North line of Township 13 North, Range 19 West, and thereby intends to, and unless enjoined by this Court will, perpetually so divert the entire flow of Rattlesnake Creek to the irreparable damage and injury of plaintiffs, and each and all of the plaintiffs.

XII.

If defendant had not attempted during the years 1931, 1932, and 1933 to change the point of diversion of the appropriation of water described in Findings of Fact Nos. 1, 2 and 9 of Cause No. 1953, and so decreed to the Missoula Water Company, to the point higher up on said stream and which is designated "Dam" on said maps, the amount of water flowing in Rattlesnake Creek at said higher up point so marked "Dam" on the maps, would have been sufficient to supply the rights to which plaintiffs were entitled and which had been decreed to their predecessors in Cause No. 1953, and also sufficient to satisfy the rights of defendant for appropriation made by defendant's predecessors at said higher up point, and at the same time there was sufficient water flowing in the stream at the head of the original Higgins ditch and at the head of [283] the Mill ditch to satisfy the appropriation described in Finding of Fact 1, 2, and 9 of Cause No. 1953; but because defendant claimed the right to change the point of diversion of the appropriation described in said Finding of Fact Nos. 1, 2 and

9 of Cause No. 1953, and attempted to divert the water to satisfy said appropriations at the place on said creek designated as "Dam" on the maps, defendant exhausted the flow of the stream at that point and at the head of plaintiff's several ditches and prevented plaintiffs from getting the water to satisfy their appropriations and at the same time caused water, at times more than 600 miner's inches flowing in the stream at the head of the Mill ditch, to run to waste. The attempted and pretended change of point of diversion, by defendant and its predecessors, did cause and is causing injury to plaintiffs.

XIII.

By the attempted change of point of diversion aforesaid, defendant is depriving plaintiffs, and all of plaintiffs, of the waters which they own and which they, and each of them, need for the irrigation of their own agricultural crops, by reason whereof plaintiffs' agricultural crops are being injured and destroyed and defendant intends and threatens to continue said attempted change of point of diversion of said water perpetually and will so continue to divert said waters to the irreparable loss of all of the plaintiffs unless enjoined by this Court. The claim of defendant to the right to change said point of diversion of water rights, which it claims, is without authority of law and is invalid.

XIV.

The appropriations of the waters of Rattlesnake Creek [284] of the plaintiffs and of each of the

plaintiffs, herein described, were accomplished and completed and many years prior in date to the pretended and attempted change of point of diversion of defendant and its predecessors in interest, from respectively the heads of the Mill ditch, original Higgins ditch and original Higgins ditch enlarged to a point near the North line of Township Thirteen North, Range 19 West; if defendant or its predecessors in interest ever acquired any right to divert any of the waters of Rattlesnake Creek at or near the last named point, such right of defendant is subsequent and junior to the rights of the plaintiffs, and each and all such rights, and is subject thereto, and defendant does not have the right to divert the waters of Rattlesnake Creek at or near the last named point at any time when the plaintiffs or any of the plaintiffs have need for the waters of said creek.

XV.

That the acts and conduct of defendant herein found and claim of defendant herein found constitute and are a cloud upon plaintiffs' right and title to their several properties; and notwithstanding that defendant's said claims and acts are without authority of law, the same interfere with the right to his property of each plaintiff and with his enjoyment thereof and plaintiffs do not have, nor has any of the plaintiffs, any plain, speedy or adequate remedy at law.

XVI.

The court finds that plaintiffs' action is not barred by the provisions of Section 9041 Revised Codes of

Montana, 1921, nor is the same barred by any provision of the Statutes of Montana; neither are plaintiffs barred nor estopped from maintaining this action because of the delay or lapse of time, [285] if any such, in the bringing thereof, and the court does expressly find against the defendant upon the plea that the plaintiffs' cause of action is barred by limitation, and likewise the court finds against the defendant upon defendant's plea that plaintiffs' cause of action is barred by reason of the laches of plaintiffs or any of the plaintiffs or their predecessors in interest or any thereof.

XVII.

That the plaintiffs were not guilty of laches, either in the commencement of their suit, or in the prosecution thereof, and that the plaintiffs' right of action set forth in the pleadings herein against the defendant is not barred by laches.

XVIII.

That the plaintiffs' action was instituted in good time and is not barred by the statute of limitations.

XIX.

Plaintiffs shall recover from defendant, costs and disbursements in this action.

From the foregoing facts the Court finds as Conclusions of Law as follows:

CONCLUSIONS OF LAW

I.

That defendant herein has the legal right to divert from Rattlesnake Creek at the place designated on the maps introduced in evidence in this cause as "Dam" to the extent that it has need therefor, the water awarded and adjudicated to its predecessors in the decree in Cause No. 1953 by rights Nos. 3, 8 and 14 of the Findings of Fact in said decree and within the limits and according to the priorities prescribed [286] in said decree, for the purpose of supplying the city of Missoula and its inhabitants with water, but defendant does not have the right to divert at said place designated on said maps as "Dam" water to satisfy any of the other decreed rights included or adjudicated by the decree in Cause No. 1953 to its predecessor in interest or to any persons and which rights have since been acquired by defendant or its predecessors, whenever plaintiffs have need for such water.

II.

That the attempt by defendant and its predecessors in interest to change the place of diversion of Right No. 1 in the Findings of Fact in the decree in Cause No. 1953 from the head of the Mill ditch to the "Dam", and likewise the attempt of defendant and its predecessors in interest, to change the place of diversion of Right No. 2, in the Findings of Fact of the decree in Cause No. 1953, from the head of original Higgins ditch to the "Dam"; and

likewise the attempt of defendant and its predecessors in interest to change the place of appropriation of Right No. 9 in the Findings of Fact of the decree in Cause No. 1953 from the head of original Higgins ditch to the "Dam" are, and each of said attempts is injurious to plaintiffs, and said attempts cause, and each said attempts caused damage and prejudice to plaintiffs and all of plaintiffs.

III.

That plaintiffs are entitled to an injunction restraining defendant from making the changes in place of diversion of the water rights described in the complaint in this action and referred to in these findings, or making either or any of such changes, whenever plaintiffs or any of [287] plaintiffs shall be unable to obtain water at his or their point of diversion on account of defendant's diversion, said plaintiff or plaintiffs then having need for such water. Particularly plaintiffs shall be entitled to enjoin and restrain defendant from changing the point of diversion of right No. 1 of the Findings of Fact in the decree in Cause No. 1953 from the head of the Mill ditch to the "Dam", and shall be entitled to enjoin and restrain defendant from changing the point of diversion of right No. 2 of the Findings of Fact of the decree in Cause No. 1953 from the head of the original Higgins ditch to the "Dam", and shall be entitled to enjoin and restrain defendant from changing the point of diversion of Right No. 9 of the Findings of Fact of the decree in Cause No. 1953 from the head of original Hig-

gins ditch to the "Dam" at any time whenever plaintiffs or any of plaintiffs have need for the water to satisfy their own appropriations and are unable to obtain the water to satisfy their own appropriations because of defendant's diversion thereof.

IV.

The claim of defendant to have the right to change the point of diversion of the water awarded and decreed to its predecessors in interest in Findings 1, 2 and 9, from the head of the Mill ditch and original Higgins ditch to the "Dam", is wrongful and without authority of law and is invalid, being injurious to plaintiffs, and defendant shall not have the right to make change of the point of diversion of said water rights, nor any thereof, whenever plaintiffs or any of plaintiffs have need for such water and are deprived of the water on account of any diversion of water by defendant. [288]

V.

That the plaintiffs were not guilty of laches, either in the commencement of their suit, or in the prosecution thereof, and that the plaintiffs' right of action set forth in the pleadings herein against the defendant is not barred by laches.

VI.

That the plaintiffs' action was instituted in good time and is not barred by the statute of limitations.

VII.

The court decides the issues herein in favor of plaintiffs and against defendant.

Let decree and judgment be entered accordingly.

Dated....., 1933.

.....
Judge. [289]

DEFENDANT'S REQUEST FOR FINDINGS
IS AS FOLLOWS:

FINDINGS OF FACT

I.

The defendant herein is the successor in interest by mesne conveyances of The Missoula Water Company, the plaintiff in Cause No. 1953 heretofore tried in the District Court of the Fourth Judicial District of the State of Montana, in and for the County of Missoula, and its predecessors, and has succeeded to all of the property of said company and its predecessors, including the water rights decreed to it in said cause.

II.

That the defendant is, and its predecessors in interest were at all times referred to in the pleadings herein, public utilities owning and operating the water system and works used to divert water from Rattlesnake Creek, the stream involved in this action, and distribute said water to the City of Missoula, Montana, and its inhabitants for fire protec-

tion and general household, domestic, irrigation, and other useful purposes, said defendant and its predecessors being authorized to engage in the sale and distribution of water, and being the owners of a franchise granted by the city of Missoula, a municipal corporation of the State of Montana, giving a perpetual right to the use of the streets and alleys of said city for pipes used to serve the said city and its people.

III.

That on the 26th day of July, 1904, final decree was duly made, given and entered in said Cause No. 1953, copy [290] of which decree is attached to the plaintiff's complaint herein, and which decree has not since been modified or set aside. That by said decree the following rights to the use of water from said Rattlesnake Creek were decreed to the defendant's predecessor:

Right No. 1, for 946" as of date 1866

“ “ 2, “ 160" as of date 1868

“ “ 3, “ 131½" as of date 1871

Part of Right No. 4,

amounting to 65" as of date 1871

Right No. 8, for 46½" as of date 1881

“ “ 9, 348" as of date 1881, and

“ “ 14, “ 645" as of date 1887.

That the following rights which were decreed in said cause to others have been acquired by the defendant's predecessors since said decree:

Part of Right No. 5,
amounting to 115" as of date 1872
Right No. 11, for 130" as of date 1882
Right No. 19, for 50" as of date 1892
Part of Right No. 20,
amounting to 65" as of date 1895, and
Part of Right No. 21,
amounting to 142" as of date 1895.

That each and all of the rights mentioned in this paragraph are and were at the time of the commencement of this action owned by the defendant.

IV.

That prior to the institution of said action No. 1953, the defendant's predecessors were the owners of said rights thereafter designated in the decree in said cause as rights numbered 1, 2 and 9, and that prior to the institution of said action defendant's predecessors diverted from said stream through what was known as the old city flume, at a point approximately one mile down stream from the present point of diversion, water sufficient to furnish a water supply to [291] the City of Missoula and its inhabitants, claiming the right to divert the water to which they were entitled from said stream for said purpose, and that this diversion and use from said point continued until the construction of the diversion works and the actual diversion referred to in the next succeeding Finding of Fact, the same being No. V.

V.

That in said cause No. 1953 The Missoula Water Company, defendant's predecessor in interest, was plaintiff and claimed certain rights to the use of water from said stream for the purpose of supplying the City of Missoula and its inhabitants, and that in the year 1902 and prior to the decree in said cause, the said predecessor in interest constructed at the point where the present diversion dam is now located upon said stream permanent diversion works, including a dam and pipe line leading to a concrete reservoir, which was connected with the distribution system supplying the city of Missoula, and during said year diverted the water necessary for furnishing said city and its inhabitants, and since said time the water required for such purpose has been continuously diverted by defendant and its predecessors at said point and the needs of the City of Missoula and its inhabitants supplied therefrom, and no water has been diverted from any other point on said stream for said purpose. That at said time in 1902 the old diversion through the said flume was discontinued.

VI.

That at the time of the construction of the diversion works mentioned in the preceding Finding and the diversion of water at said point, there was no intention upon the part of the defendant's predecessor to abandon any of the water rights [292] in said stream owned or claimed by it.

VII.

That at the time of the trial of Cause No. 1953, it was known by all of the parties thereto that diversion at the present point of the water to which defendant's predecessor was entitled from said stream to the extent necessary to supply the city of Missoula and its inhabitants, was contemplated and intended.

VIII.

That all of the plaintiffs in this action, with the exception of Missoula County, acquired such rights as they have to the use of the waters of said stream long subsequent to the time when the permanent point of diversion was established at its present location, and long subsequent to the entry of the decree in said Cause No. 1953, and that the plaintiffs herein and their predecessors in interest since the year 1902 knew that the water necessary for furnishing the city of Missoula and its inhabitants was being diverted at the present point of diversion and that they and all of them have acquiesced therein, and the defendant's water rights to the extent required have since been distributed at said point.

IX.

That by diverting the water required by defendant and its predecessors at the present point of diversion instead of at the point or points at which the same was previously diverted, no detriment or injury was or has been caused to the plaintiffs or their predecessors, and no diminution has resulted

in the amount of water available to other users on the stream. [293]

X.

That for more than thirty years immediately prior to the beginning of this action the defendant and its predecessors have diverted from Rattlesnake Creek at the point where its present diversion dam is located, the water necessary for supplying the city of Missoula and its inhabitants. That said diversion and use have been open, notorious, exclusive, continuous, and under claim of right as against plaintiffs and their predecessors and all other persons.

XI.

That the diversion at the present location of the defendant's diversion dam was made by substantial and permanent diversion works and reservoirs, and was done openly and notoriously and to the knowledge of the plaintiffs and their predecessors in interest, and that prior to the commencement of this action no action was ever brought by the plaintiffs or by any of their predecessors in interest seeking to enjoin, question or oppose the acts complained of in the present complaint. That the plaintiffs and their predecessors in interest stood by while such diversion was made and while the defendant and its predecessors in interest have expended large sums for such diversion works and for the construction and improvement thereof and the repair and improvement of the distribution system, and that during said period of time the entire system has been several times sold and transferred to new

purchasers. That during said period of time many witnesses who were familiar with the operation of said water works system and the facts and conditions existing in the year 1902, and prior thereto, and at the time such diversion was made, have died or become unavailable as witnesses, and [294] that plaintiffs and their predecessors with full knowledge have acquiesced in the diversion of water at said point and the use thereof for said purpose for more than thirty years continuously.

XII.

That neither the defendant nor its predecessors in interest have deprived the plaintiffs or their predecessors of the use of any water from Rattlesnake Creek to which they, or any of them, was or were lawfully entitled.

From the foregoing Findings of Fact, the defendant proposes the following—

CONCLUSIONS OF LAW

I.

That the defendant herein has the legal right to divert at its diversion dam in Rattlesnake Creek, being the present point of diversion, from the rights decreed to its predecessor in the decree in Cause No. 1953, and within the limits and according to the priorities prescribed in said decree, the amount of water necessary for supplying the City of Missoula and its inhabitants. That it is the owner of said rights, and none of the same has ever been abandoned.

II.

That the plaintiffs herein, and each and all of them, are barred by laches from questioning or disputing the right of the defendant so to do.

III.

That the plaintiffs herein under the facts proven and found by the court, are not entitled to any relief in equity.

DECREE ACCORDINGLY.

.....
Judge. [295]

The foregoing constitutes all the testimony introduced upon the trial of said cause and all the proceedings had upon the trial.

And now within the time allowed by law, the plaintiff and appellant lodges of the foregoing proposed statement of evidence and asks that the same be signed, settled and approved.

E. C. MULRONEY

S. P. WILSON

Attorneys for Plaintiff and
Appellant.

Lodged this.....day of April, 1934, with
the Clerk of the Above Court.

.....
Clerk of the United States District Court.

By.....

Deputy.

Service of foregoing proposed Statement of Evidence accepted by copy this 18th day of April, 1934.

MURPHY & WHITLOCK,

Of Counsel for Defendant

It is hereby stipulated and agreed between the parties to the above action be their respective attorneys that the foregoing may be signed, settled and approved as and for the statement of evidence herein.

Dated this.....day of April, 1934.

.....
Attorneys for Plaintiffs and Appellants.

.....
Attorneys for Defendant and Respondent.

CERTIFICATE OF JUDGE

I, George M. Bourquin, Judge of the above entitled Court, and the Judge before whom said cause was tried, hereby certify that the foregoing is a true and correct narrative statement of the evidence in the above entitled suit No. 1488, and that the same is now by me duly settled, allowed and approved as the statement of evidence in said cause.

BOURQUIN,
Judge.

[Endorsed]: Filed May 3, 1934. [296]

Thereafter, on May 3rd, 1934, Praeceptum for Transcript of Record was duly filed herein, in the words and figures following, to wit: [297]

[Title of Court and Cause.]

PRAECIPE.

[298]

To the Clerk of the above-entitled Court.

You will please prepare a transcript of the Record to be filed in United States Circuit Court of Appeals for the Ninth Circuit pursuant to an appeal allowed in the above-entitled cause and incorporate in such Transcript of Record the following papers or exhibits:

1. Complaint
2. Defendant's motion to dismiss
3. Minutes of the Court showing decision of motion to dismiss
4. Answer
5. Decision and opinion of Court after trial of the issues
6. Petition for allowance of appeal
7. Order allowing appeal
8. Prayer for reversal
9. Assignment of errors
10. Citation on appeal
11. Bond on appeal
12. Statement of evidence settled and approved herein.
13. This praecipe with acknowledgement of service thereon.

Said Transcript to be prepared and duly certified by you as required by law and the rules of the

above-entitled court and the rules of the United States Circuit Court of Appeals for the Ninth Circuit.

Dated this day of April, 1934.

E. C. MULRONEY and
S. P. WILSON

Attorneys for Plaintiffs.

Service of the foregoing praecipe is hereby admitted and a copy of the same received at Missoula, Montana, this 3rd day of May, 1934.

W. L. MURPHY
A. N. WHITLOCK

Attorneys for Defendant.

[Endorsed]: Filed May 3, 1934. [299]

Thereafter, on May 9th, 1934, a Counter-Praecipe for Additional Portions of the Record was filed herein, in the words and figures following, to wit:
[300]

[Title of Court and Cause.]

COUNTER-PRAECIPE

To the Clerk of the above entitled Court:

In connection with the appeal in the above entitled cause the defendant and appellee in addition to the papers and exhibits requested by the appellants to be incorporated in the transcript on appeal to be prepared by you, hereby requests that you include in such transcript the following:

1. The original decree filed in said cause.

2. The defendant's motion to adopt proposed Findings and Conclusions, together with the proposed Findings and Conclusions filed and submitted at the close of the testimony in said cause.
3. You are further requested to transmit to the Appellate Court defendant's original exhibits numbered 6 and 7.

Dated: May 8th, 1934.

MURPHY & WHITLOCK,
Attorneys for Defendant.

Service of the foregoing Counter-praecipe is hereby admitted and receipt of copy acknowledged this 8th day of May, 1934.

S. P. WILSON
E. C. MULRONEY.

[Endorsed]: Filed May 9, 1934. [302]

Thereafter, on May 9th, 1934, an Order to Transmit Certain Original Exhibits was entered herein, in the words and figures following, to wit: [303]

[Title of Court and Cause.]

ORDER

It appearing that it is necessary and proper that defendant's Exhibit No. 6, being a map introduced in evidence at the trial of the above entitled action and referred to at page 55 of the statement of the case, and defendant's Exhibit No. 7, being a chart

admitted in evidence at said trial and referred to on page 58 of said statement of the evidence, should be transmitted to the Circuit Court of Appeals of the Ninth Circuit along with the original record on appeal in the above entitled cause;

It is therefore ordered, that said original exhibits, defendant's Exhibit No. 6, and defendant's Exhibit No. 7, be transmitted by the clerk of this court to the said Appellate Court for its inspection in connection with said appeal.

Not to waive printing, unless the court waives.

Dated: May 9th, 1934.

BOURQUIN,

Judge.

[Endorsed]: Filed May 9, 1934. [305]

CERTIFICATE OF CLERK U. S. DISTRICT
COURT TO TRANSCRIPT OF RECORD.

United States of America,
District of Montana—ss.

I, C. R. Garlow, Clerk of the United States District Court for the District of Montana, do hereby certify and return to The Honorable, The United States Circuit Court of Appeals for the Ninth Circuit, that the foregoing two volumes consisting of 305 pages, numbered consecutively from 1 to 305 inclusive, constitute a full, true and correct transcript of the record and proceedings in case No. 1488, Sain, et al. vs. Montana Power Company, as appears from the original records and files of said court in my custody as such Clerk; and I do further certify and return that I have annexed to said transcript and included within said pages the original Citation issued in said cause.

And I further certify that the costs of said transcript of record amount to the sum of Fifty-one & 75/100 Dollars, (\$51.75), and have been paid by the appellants.

Witness my hand and the seal of said court at Helena, Montana, this May 25th, A. D. 1934.

[Seal]

C. R. GARLOW,

Clerk as aforesaid. [306]

[Endorsed]: No. 7499. United States Circuit Court of Appeals for the Ninth Circuit. Jackson C. Sain, Hettie Sain, Ed. Ray, Joseph H. McDonald, Missoula County, Tennie E. Greenough, Clara Pidge, W. T. Burnett, George Cromwell, Glenn Sticht, G. W. Leaphart, Josephine Youngquist, Harry E. Stetson, et al., Appellants, vs. The Montana Power Company, a Corporation, Appellee. Transcript of Record. Upon Appeal from the District Court of the United States for the District of Montana.

Filed May 28, 1934.

PAUL P. O'BRIEN

Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

United States 2
Circuit Court of Appeals
For the Ninth Circuit.

JACKSON C. SAIN, HETTIE SAIN, ED. RAY,
JOSEPH H. McDONALD, MISSOULA
COUNTY, TENNIE E. GREENOUGH,
CLARA PIDGE, W. T. BURNETT, GEORGE
CROMWELL, GLENN STICHT, G. W.
LEAPHART, JOSEPHINE YOUNGQUIST,
HARRY E. STETSON, et al.,

Appellants,

vs.

THE MONTANA POWER COMPANY,
a corporation,

Appellee.

Supplemental
Transcript of Record

Upon Appeal from the District Court of the
United States for the District of Montana.

MAR 20 1935

PAUL T. MURPHY,

United States
Circuit Court of Appeals
For the Ninth Circuit.

JACKSON C. SAIN, HETTIE SAIN, ED. RAY,
JOSEPH H. McDONALD, MISSOULA
COUNTY, TENNIE E. GREENOUGH,
CLARA PIDGE, W. T. BURNETT, GEORGE
CROMWELL, GLENN STICHT, G. W.
LEAPHART, JOSEPHINE YOUNGQUIST,
HARRY E. STETSON, et al.,

Appellants,

vs.

THE MONTANA POWER COMPANY,
a corporation,

Appellee.

Supplemental
Transcript of Record

Upon Appeal from the District Court of the
United States for the District of Montana.

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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NAMES AND ADDRESSES OF ATTORNEYS
OF RECORD.

Mr. E. C. MULRONEY,
of Missoula, Montana, and

Mr. S. P. WILSON
of Deer Lodge, Montana,
Attorneys for plaintiffs and appellants.

Mr. W. L. MURPHY
of Missoula, Montana, and

Mr. A. N. WHITLOCK
of Missoula, Montana,
Attorneys for defendant and appellee. [1*]

In the District Court of the United States
in and for the District of Montana.

No. 1488

JACKSON C. SAIN, et al.,

Plaintiffs,

vs.

THE MONTANA POWER COMPANY,
a corporation,

Defendant.

BE IT REMEMBERED that on April 25, 1934,
Decree was duly filed and entered herein, which is
in the words and figures following, to-wit: [2]

*Page numbering appearing at the foot of page of original certified
Transcript of Record.

In the District Court of the United States for the
District of Montana, Missoula Division.

No. 1488

JACKSON C. SAIN, et al.,

Plaintiffs,

vs.

THE MONTANA POWER COMPANY,
a corporation,

Defendant.

DECREE.

This cause came on to be heard at this term and was submitted by counsel for decision, and thereupon, upon consideration thereof the court filed written decision therein, and in accordance therewith IT IS ORDERED, ADJUDGED AND DECREED that said suit be dismissed without costs. Dated April 25, 1934.

BOURQUIN,

Judge.

[Endorsed]: Filed April 25, 1934. [3]

Thereafter, on July 23, 1934, Petition for Allowance of Appeal was filed herein, in the words and figures following to-wit: [4]

[Title of Court and Cause.]

PETITION FOR ALLOWANCE OF APPEAL.

[5]

The above named plaintiffs feeling themselves aggrieved by the decision, judgment and decree

entered in this cause on the 25th day of April, 1934, do hereby appeal to the Circuit Court of Appeals for the Ninth Circuit for the reasons assigned in the Assignment of Errors filed herewith and said plaintiffs pray that their appeal be allowed, and that citation issue as provided by law, and that the Transcript of Record, proceedings and papers upon which said decree was based duly authenticated, be sent to the United States Circuit Court of Appeals for the Ninth Circuit sitting in the City and County of San Francisco, State of California, under the rules of such Court in such cases made and provided.

And your petitioners further pray that a proper order touching the security to be required of them to perfect their appeal be made.

Dated this 19th day of July, 1934.

S. P. WILSON and

E. C. MULRONEY,

Attorneys for Plaintiffs.

State of Montana,
County of Missoula—ss.

Jackson C. Sain, being duly sworn upon oath says:

That he is one of the petitioners foregoing named and he makes this verification for and on behalf of all the petitioners; that he has heard read the foregoing petition and knows the contents thereof and that the matters and things therein stated are true to the best of his knowledge, information and belief.

JACKSON C. SAIN.

Subscribed and sworn to before me this 19th day of July, 1934.

[Seal] EDWARD C. MULRONEY,
Notary Public for the State of Montana, residing
at Missoula. My commission expires June
15, 1935. [6]

Service of the foregoing petition for allowance of appeal is hereby admitted and a copy of the same received at Missoula, Montana, this 23rd day of July, 1934.

W. L. MURPHY,
A. N. WHITLOCK,
Attorneys for Defendant.

[Endorsed]: Filed July 23, 1934. [7]

Thereafter, on July 23, 1934, Order Allowing Appeal was filed herein, in the words and figures, following, to-wit: [8]

[Title of Court and Cause.]

ORDER ALLOWING APPEAL. [9]

Upon reading and considering the petition for appeal on file herein together with the Assignment of Errors on file herein:

IT IS HEREBY ORDERED that the appeal of Jackson C. Sain and the other plaintiffs to the United States Circuit Court of Appeals for the Ninth Circuit be, and the same is hereby allowed,

upon the filing of a good and sufficient bond in the sum of \$300.00 to be approved by the Court.

Dated this 23rd day of July, 1934.

CHAS. N. PRAY,

Judge.

Service of the foregoing order allowing appeal is hereby admitted and a copy of the same received at Missoula, Montana, this 23rd day of July, 1934.

W. L. MURPHY,

A. N. WHITLOCK,

Attorneys for Defendant.

[Endorsed]: Filed July 23, 1934. [10]

Thereafter, on July 23, 1934, Prayer for Reversal was filed herein, in the words and figures, following, to-wit: [11]

[Title of Court and Cause.]

PRAYER FOR REVERSAL. [12]

Come now the plaintiffs in the above-entitled action and pray that the decision, judgment and decree entered herein in the District Court of the United States in and for the District of Montana on the 25th day of April, 1934, be reversed by the United States Circuit Court of Appeals for the Ninth Circuit and that such other and further orders as may be fit and proper in the premises be

made in the above-entitled cause by said Circuit Court of Appeals.

Dated this 23rd day of July, 1934.

E. C. MULRONEY and

S. P. WILSON,

Attorneys for Plaintiffs.

Service of the foregoing prayer for reversal is hereby admitted and a copy of the same received at Missoula, Montana, this 23rd day of July, 1934.

W. L. MURPHY,

A. N. WHITLOCK,

Attorneys for Defendant.

[Endorsed]: Filed July 23, 1934. [13]

Thereafter, on July 23, 1934, Assignment of Errors was filed herein, in the words and figures, following to-wit: [14]

[Title of Court and Cause.]

ASSIGNMENT OF ERRORS. [15]

Come now the plaintiffs in the above-entitled cause and file the following Assignment of Errors upon which they rely in the prosecution of their appeal from the decision, judgment and decree in said suit made and entered by the above-entitled Court on the 25th day of April, 1934.

I.

The Court erred in dismissing plaintiffs' Bill of Complaint.

II.

The Court erred in finding and holding that the Court is without jurisdiction in the cause.

III.

The Court erred in finding and holding that the State Court and not the United States Court has jurisdiction to hear and determine the matters at issue as shown by the pleadings in the cause.

IV.

The Court erred in finding and holding that to entertain this suit and decide the same in accordance with justice and the rights of the parties would constitute an invasion of the jurisdiction of the State Court.

V.

The Court erred in finding and holding that plaintiffs may not have an injunction and restraining order in this cause as prayed for in the complaint in this cause.

VI.

The Court erred in finding and deciding against the plaintiffs in this action and in favor of the defendant.

VII.

The Court erred in granting to the plaintiffs the injunction and relief prayed for in the complaint.

VIII. [16]

The Court erred in not finding each of the proposed findings of fact that were requested by the

plaintiffs, to be true, the same being numbered Findings of Fact requested by plaintiffs numbered 1 to 19, inclusive, and the Court erred in failing to find and decide that each and all of said proposed Findings of Facts are true.

IX.

The Court erred in not finding and deciding that defendant herein has the legal right to divert from Rattlesnake Creek at the place designated on the maps introduced in evidence in this cause as "Dam" to the extent that it has need therefor, the water awarded and adjudicated to its predecessors in the decree in Cause No. 1953 by rights Nos. 3, 8 and 14 of the Findings of Fact in said decree and within the limits and according to the priorities prescribed in said decree, for the purpose of supplying the city of Missoula and its inhabitants with water, but defendant does not have the right to divert at said place designated on said maps as "Dam" water to satisfy any of the other decreed rights included or adjudicated by the decree in Cause No. 1953 to its predecessors, whenever plaintiffs have need for such water.

X.

The Court erred in not finding and deciding that the attempt by defendant and its predecessors in interest to change the place of diversion of Right No. 1 in the Findings of Fact in the decree in Cause No. 1953 from the head of the Mill ditch to the "Dam", and likewise the attempt of defendant and

its predecessors in interest, to change the place of diversion of Right No. 2, in the Findings of Fact of the decree in Cause No. 1953, from the head of original Higgins ditch to the "Dam"; and likewise the attempt of defendant and its predecessors in interest to change the place of appropriation of Right No. 9 in [17] the Findings of Fact of the decree in Cause No. 1953 from the head of original Higgins ditch to the "Dam" are, and each of said attempts is, injurious to plaintiffs, and said attempts cause, and each said attempts causes, damage and prejudice to plaintiffs and all of plaintiffs.

XI.

The Court erred in not finding and deciding that plaintiffs are entitled to an injunction restraining defendant from making the changes in place of diversion of the water rights described in the complaint in this action and referred to in these findings, or making either or any of such changes, whenever plaintiffs or any of plaintiffs shall be unable to obtain water at his or their point of diversion on account of defendant's diversion, said plaintiff or plaintiffs then having need for such water. Particularly plaintiffs shall be entitled to enjoin and restrain defendant from changing the point of diversion of right No. 1 of the Findings of Fact in the decree in Cause No. 1953 from the head of the Mill ditch to the "Dam", and shall be entitled to enjoin and restrain defendant from changing the point of diversion of right No. 2 of the Findings of Fact of the decree in Cause No. 1953 from the head of the

original Higgins ditch to the "Dam", and shall be entitled to enjoin and restrain defendant from changing the point of diversion of Right No. 9 of the Findings of Fact of the decree in Cause No. 1953 from the head of original Higgins ditch to the "Dam", at any time whenever plaintiffs or any of plaintiffs have need for the water to satisfy their own appropriations and are unable to obtain the water to satisfy their own appropriations because of defendant's diversion thereof.

XII.

The Court erred in not finding and deciding the claim of defendant to have the right to change the point of diversion [18] of the water awarded and decreed to its predecessors in interest in Findings 1, 2 and 9, from the head of the Mill ditch and original Higgins ditch to the "Dam", is wrongful and without authority of law and is invalid, being injurious to plaintiffs, and defendant shall not have the right to make change of the point of diversion of said water rights, nor any thereof, whenever plaintiffs, or any of plaintiffs, have need for such water and are deprived of the water on account of any diversion of water by defendant.

XIII.

The Court erred in not finding and deciding that the plaintiffs were not guilty of laches, either in the commencement of their suit, or in the prosecution thereof, and that the plaintiffs' right of action set forth in the pleadings herein against the defendant is not barred by laches.

XIV.

The Court erred in not finding and deciding that the plaintiffs' action was instituted in good time and is not barred by the statute of limitations.

XV.

The Court erred in not finding and deciding the issues herein in favor of plaintiffs and against defendant.

WHEREFORE, plaintiffs pray that the decree herein be reversed.

E. C. MULRONEY and
S. P. WILSON,

Attorneys for Plaintiffs.

Service of the within Assignment of Errors is hereby admitted and a copy thereof received at Missoula, Montana, this 23rd day of July, 1934.

W. L. MURPHY,
A. N. WHITLOCK,

Attorneys for Defendant.

[Endorsed]: Filed July 23, 1934. [19]

Thereafter, on July 23, 1934, Bond on Appeal was filed herein, in the words and figures following, to-wit: [20]

[Title of Court and Cause.]

BOND ON APPEAL. [21]

KNOW ALL MEN BY THESE PRESENTS:

That we, Jackson C. Sain, in his own behalf and on behalf of all the plaintiffs above named, as prin-

cipal, and Chas. Ferguson, of Missoula, Montana, by occupation a real estate broker, and Abbon M. Lucy, of Missoula, Montana, by occupation a merchant, are held and firmly bound unto Montana Power Company, a corporation, the defendant above named in the full sum of Three Hundred Dollars, to be paid to the said defendant, its successors or assigns to which payment well and truly to be made, said principal and said sureties bind themselves, their, and each of their, successors and assigns, jointly and severally, firmly by these presents.

Sealed and dated this 19th day of July, 1934.

WHEREAS, in the District Court of the United States for the District of Montana in the above-entitled suit pending in said Court between the above named plaintiffs and the above named defendant, a decision, judgment and decree was rendered against the plaintiffs upon the 25th day of April, 1934, which judgment was entered on the 25th day of April, 1934, and said plaintiffs have petitioned for an appeal from said decision, judgment and decree to the Circuit Court of Appeals of the United States for the Ninth Circuit and said plaintiffs propose to prosecute said appeal to reverse the said decision, judgment and decree and answer all costs if they fail to make their plea good.

NOW, THEREFORE, in consideration of said appeal, the condition of this obligation is such that if the plaintiffs shall prosecute their said appeal to effect and answer all costs if they fail to make good

their plea, then this obligation shall be void, otherwise to remain in full force and effect.

JACKSON C. SAIN,
CHAS. FERGUSON,
ABBON M. LUCY. [22]

State of Montana,
County of Missoula—ss.

Chas. Ferguson and Abbon M. Lucy, the sureties named in the above bond, being duly sworn, each for himself, says that he is a free holder and resident within said Missoula County, Montana, and is worth the said sum of Three Hundred Dollars over and above all his debts and liabilities, exclusive of property exempt from execution.

CHAS. FERGUSON,
ABBON M. LUCY.

Subscribed and sworn to before me this 23rd day of July, 1934.

[Seal] EDWARD C. MULRONEY,
Notary Public for the State of Montana, residing
at Missoula, Montana. My commission expires
June 15, 1935.

The foregoing bond approved this 23rd day of July, 1934.

CHAS. N. PRAY,

Judge.

[Endorsed]: Filed July 23, 1934. [23]

Thereafter, on July 23, 1934, Citation was duly issued herein, which original Citation is hereto annexed and is in the words and figures following, to-wit: [24]

[Title of Court and Cause.]

CITATION. [25]

United States of America to Montana Power Company, a Corporation, GREETING:

You are hereby cited and admonished to be and appear in the United States Circuit Court of Appeals for the Ninth Circuit to be held at the City of San Francisco, California, which thirty days of the date hereof pursuant to an order filed and entered in the office of the Clerk of the District Court of the United States for the District of Montana, allowing an appeal from a decision, judgment and decree filed and entered in said Court on the 25th day of April, 1934, in favor of the defendant and against the plaintiffs in the above-entitled action being In Equity Number 1488, wherein you are the defendant and the above named plaintiffs are the plaintiffs, to show cause, if any there be, why the decision, judgment and decree rendered against the said plaintiffs, as in said appeal mentioned, should not be reversed and corrected and why justice should not be done the parties in that behalf.

WITNESS the Honorable Judge of the United States District Court for the District of Montana, the 23rd day of July, 1934.

CHARLES N. PRAY,

Judge.

Service of the foregoing citation admitted and a copy thereof received at Missoula, Montana this 23rd day of July, 1934.

MURPHY & WHITLOCK,
Attorneys for Defendant.

[Endorsed]: Filed July 27, 1934. [26]

Thereafter, on August 22, 1934, Stipulation for Supplemental Transcript of Record was filed herein, in the words and figures, following, to-wit: [28]

[Title of Court and Cause.]

STIPULATION. [29]

WHEREAS, in this cause plaintiffs took and perfected an appeal from the decision of the Court dated and filed on February 5th, 1934, and plaintiffs, as appellants, caused a transcript on appeal to be prepared and filed with the Clerk of the Circuit Court of Appeals, Ninth Circuit, wherein is set forth the pleadings in this cause and proceedings upon the trial and the testimony of the witnesses together with the proceedings taken in perfecting said appeal;

AND WHEREAS, a decree was signed, dated and filed upon April 25th, 1934, and the plaintiffs, desiring to appeal from said judgment of date April 25th, 1934, have petitioned for the allowance of an appeal and such an appeal has been allowed by the above court by an order of allowance of appeal of date July 23rd, 1934;

AND WHEREAS, the parties hereto, both plaintiffs and defendant, desire to avoid any needless repetition or duplication of the record or transcript on appeal in this cause and do make and enter into this stipulation with the view of, and for the purpose of, avoiding the necessity of preparing another transcript on appeal, or rewriting, or duplicating, the transcript of record already prepared and filed as aforesaid.

NOW THEREFORE, it is stipulated and agreed between the parties hereto, by their respective attorneys, that the transcript of record already prepared and filed herein and served by appellants upon appellee shall, together with copies of the decree dated and signed April 25, 1934, Petition for Allowance of Appeal, Order Allowing Appeal, Prayer for Reversal, Assignment of Errors, Citation and Bond on Appeal, Praecipe to Clerk and this Stipulation constitute the record on appeal from the judgment of April 25th, 1934, which said papers shall be printed as supple- [30] mental transcript on appeal.

Dated August 21st, 1934.

E. C. MULRONEY and
S. P. WILSON,

Attorneys for Appellants.

W. L. MURPHY and
A. N. WHITLOCK,

Attorneys for Appellee.

[Endorsed]: Filed Aug. 22, 1934. [31]

Thereafter, on August 22, 1934, Praecipe for Supplemental Transcript of Record was filed herein, in the words and figures following, to-wit: [32]

[Title of Court and Cause.]

PRAECIPE. [33]

To the Clerk of the above-entitled Court:

You will please prepare a Transcript of the Record to be filed in United States Circuit Court of Appeals for the Ninth Circuit pursuant to an appeal from the judgment dated April 25th, 1934, which appeal is duly allowed in the above-entitled cause, and you will please incorporate in such Transcript of Record the following papers, to-wit:

1. Stipulation entered into between plaintiffs in this action and the defendant, by their respective attorneys, which stipulation bears date August 21st, 1934.

2. Decree dated and filed April 25th, 1934.

3. Petition for allowance of appeal.

4. Order allowing appeal.

5. Prayer for reversal.

6. Assignment of errors.

7. Citation on appeal.

8. Bond on appeal.

9. This praecipe with acknowledgment of service thereon.

Said Transcript to be prepared and duly certified by you as required by law and the rules of the above-entitled court and the rules of the United

States Circuit Court of Appeals for the Ninth Circuit.

Dated this 21st day of August, 1934.

E. C. MULRONEY and

S. P. WILSON,

Attorneys for Plaintiffs.

Service of the foregoing praecipe is hereby admitted and a copy of the same received at Missoula, Montana, this 21st day of August, 1934.

W. L. MURPHY,

A. N. WHITLOCK,

Attorneys for Defendant.

[Endorsed]: Filed Aug. 22, 1934. [34]

CERTIFICATE OF CLERK U. S. DISTRICT
COURT TO TRANSCRIPT OF RECORD.

United States of America,
District of Montana.—ss.

I, C. R. Garlow, Clerk of the United States District Court for the District of Montana, do hereby certify and return to The Honorable, The United States Circuit Court of Appeals for the Ninth Circuit, that the foregoing volume consisting of 34 pages, numbered consecutively from 1 to 34 inclusive, constitute full, true and correct copies and transcript of the following parts of the record in case No. 1488, Sain, et al. vs. Montana Power Company, as appears from the original records and files of said court in my custody as such Clerk, to-wit:

1. Stipulation entered into between plaintiffs in this action and the defendant, by their respective attorneys, which stipulation bears date August 21st, 1934.
2. Decree dated and filed April 25th, 1934.
3. Petition for allowance of appeal dated and filed July 23rd, 1934.
4. Order allowing appeal dated and filed July 23rd, 1934.
5. Prayer for reversal dated and filed July 23rd, 1934.
6. Assignment of errors dated and filed July 23rd, 1934.
7. Citation on appeal dated July 23rd, 1934.
8. Bond on appeal dated and filed July 23rd, 1934.
9. Praecipe with acknowledgment of service thereon filed August 22nd, 1934.

I do further certify that the foregoing documents are prepared to constitute a Transcript of Record upon appeal from said judgment of date April 25th, 1934 and that I have annexed to said transcript and included within said pages the original Citation issued in said cause.

And I further certify that the costs of said transcript of record amount to the sum of Three and 50/100 Dollars (\$3.50), and have been paid by the appellants. [35]

Witness my hand and the seal of said court at Helena, Montana, this August 22nd, A. D. 1934.

[Seal]

C. R. GARLOW,

Clerk as aforesaid. [36]

[Endorsed]: No. 7499. United States Circuit Court of Appeals for the Ninth Circuit. Jackson C. Sain, Hettie Sain, Ed. Ray, Joseph H. McDonald, Missoula County, Tennie v. Greenough, Clara Pidge, W. T. Burnett, George Cromwell, Glenn Sticht, G. W. Leaphart, Josephine Youngquist, Harry E. Stetson, et al., Appellants, vs. The Montana Power Company, a corporation, Appellee. Supplemental Transcript of Record. Upon Appeal from the District Court of the United States for the District of Montana.

Filed August 24, 1934.

PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of Appeals
for the Ninth Circuit.

IN THE

United States

Circuit Court of Appeals

FOR THE NINTH CIRCUIT

Missoula Division

JACKSON C. SAIN, HETTIE SAIN, ED RAY,
JOSEPH H. McDONALD, MISSOULA COUNTY,
TENNIE E. GREENOUGH, CLARA PIDGE, W.
T. BURNETT, GEORGE CROMWELL, GLENN
STICHT, G. W. LEAPHART, JOSEPHINE
YOUNGQUIST, HARRY E. STETSON, A. M.
ROGERS, I. E. PETERSON, H. E. STURM, MIN-
NIE L. McCANN, A. L. KAGLE, ISRAEL Q. ROB-
ERTS, WILLIAM J. JOHNSON, HORACE A.
GREEN, PEARL GREEN, W. D. SATTERFIELD,
MARGARET A. SATTERFIELD, E. F. ROTH,
ELLEN R. WHITING, L. A. WAGONER,
CHARLES E. LUCAS, CHARLES A. MARTIN-
SON and FREDA MARTINSON, co-partners doing
business under the firm name of MISSOULA ICE
COMPANY, ORPHA MILLER TALBOTT, and
RUSSELL H. MILLER,

Appellants, Plaintiffs Below,

vs.

THE MONTANA POWER COMPANY, A CORPO-
RATION,

Appellee, Defendant Below.

Appellants' Brief

E. C. MULRONEY,
Missoula, Montana,

S. P. WILSON,
Deer Lodge, Montana,
Attorneys for Appellants.

FILED

AUG 27 1934

PAUL P. GIBSON,
CLERK

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IN THE

United States

Circuit Court of Appeals

FOR THE NINTH CIRCUIT

Missoula Division

JACKSON C. SAIN, HETTIE SAIN, ED RAY,
JOSEPH H. McDONALD, MISSOULA COUNTY,
TENNIE E. GREENOUGH, CLARA PIDGE, W.
T. BURNETT, GEORGE CROMWELL, GLENN
STICHT, G. W. LEAPHART, JOSEPHINE
YOUNGQUIST, HARRY E. STETSON, A. M.
ROGERS, I. E. PETERSON, H. E. STURM, MIN-
NIE L. McCANN, A. L. KAGLE, ISRAEL Q. ROB-
ERTS, WILLIAM J. JOHNSON, HORACE A.
GREEN, PEARL GREEN, W. D. SATTERFIELD,
MARGARET A. SATTERFIELD, E. F. ROTH,
ELLEN R. WHITING, L. A. WAGONER,
CHARLES E. LUCAS, CHARLES A. MARTIN-
SON and FRED A. MARTINSON, co-partners doing
business under the firm name of MISSOULA ICE
COMPANY, ORPHA MILLER TALBOTT, and
RUSSELL H. MILLER,

Appellants, Plaintiffs Below,

vs.

THE MONTANA POWER COMPANY, A CORPO-
RATION,

Appellee, Defendant Below.

No. 1488

APPELLANTS' BRIEF

I.

STATEMENT OF THE CASE

This suit is in equity. It involves the use of the waters of Rattlesnake Creek in Missoula County, Montana. The court obtains jurisdiction because of the

diversity of citizenship, appellants, plaintiffs below, being all citizens of Montana and appellee, defendant below, being a corporation organized and existing under the laws of the State of New Jersey; the matter in controversy exceeding, exclusive of interest and costs, the sum and value of Three Thousand Dollars.

Upon the 9th day of July, 1903, a judgment was rendered in the District Court of Missoula County, Montana, being Cause No. 1953, bearing date on that day, adjudicating the waters of said Rattlesnake Creek between appropriators and determining the respective rights, priorities, and amounts which the several appropriators were entitled to use and thus Rattlesnake Creek became an adjudicated stream as defined by Section 7128, Revised Codes of Montana, 1921. (Tr., 43-55, Ex. "A.") The judgment, though dated July 9, 1903, seems to be marked "Filed" in the month of July, 1904. Such manifestly was the result of an inadvertence or oversight in the office of the Clerk of the Court because the register of actions introduced in evidence (Tr., 142) shows that immediately after the date of the judgment, namely, July 3, 1903, a motion for a new trial was made, considered, and denied (Tr., 148); as we know, the motion for a new trial could not have preceded the entering of the judgment in the case. If it makes any difference at all whether the judgment was rendered upon July 3, 1903, or in July, 1904, then it must be apparent that the same was rendered upon the day it bears date. Appellants can see no material difference as to whether the rendition of this judgment

was the former, or the latter, date and hence will not discuss the point further.

Appellee in this action is the successor of the plaintiff in Cause No. 1953; appellants are the successors of many, though not all, of the defendants in Cause No. 1953. The respective interests of appellants and appellee, and that they are, respectively, successors to parties in Cause No. 1953 is fully established by proof and by agreement of counsel. (Tr., 65; Tr., 165.) In Cause No. 1953 the court made twenty-three separate findings of fact; in each such finding of fact there is awarded a right to some one or more of the parties, plaintiffs or defendant. Priority of rights runs in the numerical order, hence, precise date of appropriations need not be retained. Conclusions of Law in accordance therewith were also made.

Plaintiff in Cause No. 1953, predecessor of appellee here, was awarded the following rights (Tr., 80):

1. 946 inches April 1, 1866, *by what is called the Mill Ditch, for mechanical, power and other beneficial purposes, and that the same has been used by plaintiff and its predecessors in interest ever since, and that no part thereof has ever been abandoned.*

2. 160 inches November 16, 1868, *by what is called the original Higgins Ditch, and that no part of said appropriation has ever been abandoned.*

9. 348 inches May 1, 1881, enlarged the original Higgins Ditch—to 508 inches thereby making an additional appropriation of—348 inches—and *that no part thereof has ever been abandoned.*

While the rights of the several appellants are separate and several, for the purposes of this action the same may be considered as one group or a single right; so considered appellants succeed to the following decreed rights fixed in Cause No. 1953, to-wit:

- 45 inches of Right 5, Williams Ditch;
- 145 inches of Right 10, Hollenback Ditch;
- 50 inches of Right 16, Hollenback Ditch;
- 100 inches of Right 17, Effinger Ditch;
- 50 inches of Right 18, Niell Ditch;
- 248 inches of Right 20, Quast Ditch;
- 127.3 inches of Right 21, Cobban-Raymond Ditch;
- 55 inches of Right 22, Hamilton Ditch.

It is established by the pleadings and the admissions that, in addition to the Right 1, 2, and 9, directly involved here, appellee has also the following rights:

- 13½ inches of Right 3 for city water works purposes;
- 65 inches of Right 4, Fredline Ditch;
- 115 inches of Right 5, Williams Ditch;
- 46½ inches of Right 8, city water works purposes;
- 130 inches of Right 11, Federson Ditch;
- 645 inches of Right 14, city water works purposes;
- 50 inches of Right 19, Duncan right;
- 65 inches of Right 20, Quast Ditch;
- 142 inches of Right 21, Cobban-Raymond Ditch.
(Tr., 80-81.)

The entire flow of Rattlesnake Creek at low water time measures 1642.32 miners inches (Tr., 136) which is average flow. (Tr., 167.)

II.

THE PLEADINGS

The complaint alleges that Right No. 1 was appropriated through the Mill Ditch taking water from Rattlesnake Creek at its lower end and near the mouth of the creek, for water power and mill purposes, which use was continued down to and subsequent to the rendition of the judgment in Cause No. 1953; that Rights 2 and 9 were both appropriated through the original Higgins Ditch for irrigation, tapping Rattlesnake Creek about a mile above the mouth of Rattlesnake Creek; that these points of diversion are some distance below the points where the several rights of the plaintiffs have always been diverted. It is alleged that subsequent to the decree in Cause No. 1953, appellee's predecessors abandoned the appropriations 1, 2, and 9 and ceased using the water appropriated through these ditches, but that appellee's predecessors, without right, diverted an amount of water equal to the amount of these appropriations at a point higher up on the stream and in the vicinity of the places of diversion of the several appellants; appellants complain that water to supply the appropriations through the Mill Ditch and the original Higgins Ditch arose in the bed of the stream and along its course below appellants' several points of diversion and that, notwithstanding the diversions by the several appellants, there always was, and is water flowing in Rattlesnake Creek sufficient to supply the

Mill Ditch and original Higgins Ditch appropriations. In other words, that the priority of the Mill Ditch and original Higgins Ditch would not have interfered with the several appropriations of appellants because, notwithstanding such appropriations, there is still flowing in Rattlesnake Creek at the heads of the Mill Ditch and the original Higgins Ditch sufficient water to supply the appropriations for those ditches, and which water, when not diverted to supply the appropriations through those ditches, flows to waste to the mouth of the creek and into the Hellgate River. By assuming the right to divert the Mill Ditch and original Higgins Ditch appropriations at the higher-up point, marked on maps as "Dam," appellee, in low water time and when most needed by appellants, takes practically the entire flow of the creek to supply its needs, thus depriving appellants of the use of the water and at the same time the amount flowing in the creek below appellants' several points of diversion flows to waste past the head of the Mill Ditch and original Higgins Ditch. Appellants claim that the pretended and attempted change of point of diversion is injurious to them and causes them prejudice. (Tr., 34-41, Complaint, para. XII-XX.)

The answer admits that Rights No. 1, 2, and 9 were originally appropriated through, respectively, the Mill Ditch and original Higgins Ditch (Tr., 62-63, para. VI), and likewise that these waters were originally diverted and used through these ditches; defendant's Answer also asserts that after the original appropriations the defendant, desiring to divert all its water at a

single point of diversion, did change the place of diversion of these appropriations from the head of the Mill Ditch and Original Higgins Ditch to its dam, located and described in its Answer and by the testimony. In other words, it is established by the pleadings that these rights here complained of, namely 1, 2, and 9, though originally appropriated for the Mill Ditch and original Higgins Ditch and diverted for a long period of time through those ditches, were subsequently transferred to the point higher up on the stream above and in the vicinity of the point of diversion of the several appellants, and appellee, having affirmed the assertion that it had changed the points of diversion of these rights, asserts its right to continue to divert the water at the new point of diversion as superior to any right to the use of the waters of any of appellants. Appellee also pleads that it has acquired the right to continue this change of point of diversion because it has adversely asserted the right for a period exceeding the period of the statute of limitations and that defendant has expended substantial and large sums of money in perfecting its works for the profitable enjoyment of its enterprise of furnishing water to the City of Missoula, and appellants are barred and precluded by the statute of limitations and laches from maintaining this action. (Tr., 79-93.) Appellee claims that the change of point of diversion did not increase, but lessened, the burden upon the stream. (Tr., 85, para. V.)

III.

THE TESTIMONY

W. H. Swearingen prepared a map (Tr., 119, Ex. 1) of Rattlesnake Creek area showing in a general way the holdings of the several plaintiffs and their places of diversion of water from Rattlesnake Creek, showing, also, the original point of diversion through the Mill Ditch and the Higgins Ditch. These various points were shown to the witness by Will Cave, an old time resident of the community, familiar with the points from the early days (Tr., 116), and the "Dam" where appellee now asserts the right to make its diversion of the water originally diverted through the Mill Ditch and the Higgins Ditch respectively. (Tr., 117-119.) Appellee's Exhibit 6 (Tr., 179) is a map showing substantially the same things. There are no tributaries coming into Rattlesnake Creek below the "Dam" (Tr., 169) and the maps, Exhibits 1 and 6, show all the ditches leading from the stream. The "Dam" where appellee seeks to divert the water for distribution to the City of Missoula is approximately three miles up stream from the head of the Mill Ditch and two miles up stream from the head of the Higgins Ditch. (Tr., 180.) The irrigation ditches of appellants tapped the stream at points near the "Dam," some of them a short distance above and others a short distance below, Exhibits 1 and 6. The testimony clearly shows that the various diversions at, and in the immediate vicinity of, the "Dam" exhaust the entire flow of the stream dur-

ing the months of July and August. (Tr., 121; Tr., 128; Tr., 130; Tr., 162.) In the year 1926, and on account of the seeming encroachment of the water company upon the rights of the agricultural appropriators, a group of the agricultural appropriators placed a weir in the creek where the Mill Ditch takes out. (Tr., 121.) During the months of July and August of that year various measurements were made by their weir. At the time of such measurements, invariably, the stream was dry immediately below the "Dam," but that by reason of the water rising in the bed of the stream below the points of diversion of appellants and above the heads of the Higgins Ditch and the Mill Ditch, a substantial flow was measured over the weir. (Tr., 122; Tr., 126; Tr., 130; Tr., 167; Tr., 162.) The result, thus indicated by the measurements, is only illustrative of the condition every year. (Tr., 139; Tr., 163; Tr., 165; Tr., 137; Tr., 168.) The water flowing where the weir was placed went to waste, the same not being available for use by appellants and not actually used by appellee to supply any of its decreed rights. The weir installed was a ten foot weir (Tr., 126; Tr., 167) and the measurements indicated a flow of $4\frac{1}{2}$ inches in depth over the weir, which would be 304 miners inches of water (Tr., 136) to as much as $7\frac{1}{2}$ inches in depth of water going over the weir, which would exceed a flow of 600 inches, all of which water was in the bed of the stream at the place where the weir was installed and all of which flowed to waste. There was also always a substantial flow going through the Fredline Ditch constituting also water ris-

ing in the bed of the stream and amounting to as much as 250 inches (Tr., 280) and which would have been available to supply the Mill Ditch appropriation if such appropriation were still diverted through the Mill Ditch. (Tr., 171; Tr., 163; Tr., 137-138; Tr., 124-125.)

The entire flow of Rattlesnake Creek is necessary to supply the needs of the various appropriators and the entire flow is applied to beneficial uses, when available, and whenever the water is wasted, such wasting results in substantial damage and injury to appellants. (Tr., 169; Tr., 165.) In the year 1931, at the height of the irrigation season, the ditches of all the appellants were closed and the entire flow of the stream at the "Dam" diverted by appellee (Tr., 165; Tr., 162; Tr., 137) and thus the agricultural appropriators were deprived of the use of the water. One of the appellants testified to having entirely suspended his own farming during the year 1931 because of his water being shut off and of going to work out in another locality. (Tr., 165.) Partial deprivation is shown during earlier years by practically all the agricultural appropriators. There is no substantial dispute to any of this testimony, nor can it be successfully urged from the record in this case but that appellants would have received water from the stream if appellee would accept the water decreed for Rights 1, 2, and 9 at the heads of the Mill Ditch and Higgins Ditch, respectively.

Surveyor Ray (Tr., 136), at the instance of Tucker, upon August 7, 1924, made an exact and precise meas-

ure of the entire flow of the stream just above the “Dam” and found it to be 1642.32 miners inches of water. Witness Tucker explains (Tr., 167; Tr., 136) that the flow then was a normal flow for that time of year and that it was a low water point of the year. Appellee’s superintendent, Christenson, testified to a minimum flow for the stream, in low water time, of 1400 inches. (Tr., 211.) This witness had made numerous measurements upon the stream and was thoroughly familiar with the volume of such flow. It is fairly established that 1600 miners inches is the approximate minimum flow of the stream.

Other than the water rights decreed for the Mill Ditch and the Higgins Ditch, appellee owns the following decreed rights:

- Right 3, 131½ inches, city water works purposes;
- Right 8, 461½ inches, city water works purposes;
- Right 14, 645 inches, city water works purposes.

A total of 705 inches. These rights were all decreed in Cause No. 1953 to appellee’s predecessor for water works purposes and, at the time of the decree, were being diverted at a point just below where the “Dam” is now located. Appellee has Rights Nos. 3, 8, and 14 and the unquestionable right to divert the same at the “Dam.” The aggregate of these rights being 705 inches, and there is no dispute nor contest of appellee’s right to divert the amount of these three appropriations for water works purposes at the “Dam.” Taking then the normal flow during low water period, say during the month of August, to be 1600 inches, and the normal

needs of appellee to be 700 inches, there remains at the dam 900 inches to be used to satisfy appellants' appropriations; these aggregate 820 inches. The result shows water sufficient to supply the needs of all parties. At the same time there is an excess of flow at the dam, which, together with the water rising in the bed of the stream, is available to meet any need at the head either of the Mill Ditch or the original Higgins Ditch. Contrast this with the undisputed situation occurring in 1931 when appellee, claiming the right to change its point of diversion, took No. 1, Mill Ditch, and No. 2 and No. 9, original Higgins Ditch, or so much thereof as they chose to take, at the dam, thus exhausting the stream and entirely depriving all the appellants of the use of the water. At the same time, more than 600 inches was flowing to waste to the mouth of the stream, or out the Fredline Ditch. Clearly, during any normal year there is not sufficient water at the dam to supply appellee's claim to divert at that point Right 1, 946 inches; Right 2, 160 inches; Right 3 and 8, 60 inches; Right 9, 348 inches; Right 14, 645 inches; a total of 2159 inches, and at the same time meet the decreed rights of appellants, aggregating 820.3 inches. Yet, during such years there will be 600 inches, or thereabouts, flowing to waste at the head of the Mill Ditch, benefiting no one. But for appellee's asserted right to change its place of diversion, there would be sufficient water at the dam to supply its water works appropriations, 705 inches, and also appellants' appropriations, 820.3 inches, and a surplus to satisfy original Higgins

Ditch and Mill Ditch appropriations rising in the bed of the stream above those ditches. Thus, it is conclusively shown that the change in the point of diversion resulted in prejudice to the agricultural appropriators. The "Dam" is 305 feet higher in elevation than the head of the Mill Ditch. (Tr., 300.)

IV.

At the conclusion of the trial, the request was made and leave granted to each side to file a request for Findings of Fact and Conclusions of Law (Tr., 302) and the Findings requested by appellants are set forth (Tr., 302) while those requested by appellee are set forth (Tr., 319), and the cause was submitted on October 26, 1933. The decision of the court below was rendered upon February 5, 1934 (Tr., 97) and the Facts are found to be as follows:

Sain, et al., vs. Montana Power Company, No. 1488, Federal Supplement 792.

"Ignoring nonessentials of strategy, camouflage, and nuisance-value, the gist of the case is whether defendant's change in place of diversion of water inflicts substantial injury on any plaintiff.

The evidence discloses appropriations by defendant in amount 1,184 inches prior to any plaintiff's, 169 inches more, prior to any plaintiff's save one of 45 inches, 775 inches more, prior to any plaintiff's save the aforesaid and one of 145 inches, and some subsequent unnecessary to detail.

The change involved, made in 1902, is from the Mill ditch and the Higgins ditch, both below plain-

tiffs, to a dam $1\frac{3}{4}$ miles above the Mill and 100 feet higher, and above most of plaintiffs.

The defendant is a public utility and now diverts no water save at said dam and to serve the city of Missoula. It appears defendant has not diverted more than 1,112 inches, or 6 inches more than its appropriations by the ditches aforesaid and prior to all plaintiffs.

Above the dam defendant has eight reservoirs, but claims nothing here by reason of any excess water stored. The dam obstructs all flow of the stream save overflow more or less intermittent and which varies as varies the flow and diversion by defendant. Likewise varies the flow below the dam.

Taking the testimony for it and particularly that of defendant's superintendent, when defendant sometimes diverts all flow, the surface flow runs off and the bed of the creek dries to a short distance above the Higgins ditch. There and below, however, the usual surface flow emerges, and always affords a surface flow of water at the head of at least the Mill ditch, in amount sometimes 340 inches.

In effect, the subsurface operates as a bypass around plaintiffs' places of diversion, and as a tributary or accretion to the stream above defendants before the change. This water not available to defendant at the Mill ditch if not at the Higgins ditch, is by it permitted to waste and its equivalent taken at the dam.

And this consequence of the change is the grievance and injury of which plaintiffs complain. That complaint is justified, grievance and injury real and substantial is clear, plain as a pike staff.

A single illustration suffices.

Assume a flow of 1,000 inches at the dam, defendant's need and diversion 700 inches, and over-

flow 300 inches. The last enters the subsurface and only emerges where unavailable to any plaintiff but available to defendant. Obviously, had defendant not changed diversion from the ditches to the dam, the 1,000 inches in surface and subsurface flow adown the stream would supply 300 inches to plaintiffs and 700 inches, its need and so the limit of its right, to defendant at the ditches. Therefore, at that time or any other of shortage, in just apportionment this wasted water is to be charged against defendant, its diversion at the dam limited to its need (in general, always the limit of a water right when others need water, however greater the appropriation), less any substantial flow at the head of the Higgins and/or the Mill ditch, the deduction not to exceed the extent of defendant's resort to the priorities by said ditches obtained."

V.

QUESTIONS INVOLVED

1. At the bringing of the action, the primary questions involved were:

(a) Are appellants injured by the attempted change of point of diversion; and

(b) Notwithstanding such injury, have appellants, by laches or by the running of the statute of limitations, lost their right to object to the change of point of diversion?

If it can be said that there was any substantial conflict in the evidence as to such questions, all such conflict is set at rest by the decision of the court below. The decision clearly and unqualifiedly finds the facts in favor of appellants. Not only must it be said that the

decision below is sustained by substantial testimony, but appellants urge such findings are the only reasonable result to be gathered from the testimony and the same are overwhelmingly supported by the testimony produced upon the trial.

2. After finding the facts thus clearly in favor of appellants, the court below continuing found and it is true that in 1903 a decree was rendered in the State court of the county where this stream is situated settling priorities in time and amount and enjoining each party thereto from trespassing upon the right of the other; that since the rendition of such decree, the court rendering the same still maintains and exercises jurisdiction to enforce and execute such decree by its officer (water commissioner) to apportion the water and supervise its use. The court decides that appellants' rights must be vindicated, if at all, by the State court and that appellants may not seek an injunction in this court but that the acts complained of by appellants, if and to the extent the same may be wrongful, justify a penalty on the appellee from the state court. In effect, that the relief sought by appellants in this action is only such as may be extended by the state court where the water rights in question were adjudicated. The court below further decided that, by virtue of having adjudicated the water rights upon Rattlesnake Creek by the decree of 1903, the state court obtained exclusive jurisdiction over the subject-matter of the action and should proceed to the determination of such water rights without interference by any other court;

that, for this court to enter a decree in this case upon the merits, would constitute an invasion of the jurisdiction of the state court. The court ordered this case dismissed.

VI.

SPECIFICATION OF ERRORS

1. The court erred in rendering the decision of February 5th, 1934, and dismissing appellants' Bill of Complaint.

2. The court erred in finding and holding that the court is without jurisdiction in the cause.

3. The court erred in finding and holding that the State Court and not the United States Court has jurisdiction to hear and determine the matters at issue as shown by the pleadings in the cause.

4. The court erred in finding and holding that to entertain this suit and decide the same in accordance with justice and the rights of the parties would constitute an invasion of the jurisdiction of the State Court.

5. The court erred in finding and holding that appellants may not have an injunction and restraining order in this cause as prayed for in the complaint in this cause.

6. The court erred in finding and deciding against the appellants in this action and in favor of the defendant.

7. The court erred in granting to the appellants the injunction and relief prayed for in the complaint.

8. The court erred in not finding each of the proposed findings of fact that were requested by the appellants, to be true, the same being numbered Findings of Fact requested by appellants numbered 1 to 19 (Tr., 302-315), inclusive, and the court erred in failing to find and decide each and all the conclusions of law requested by appellants numbered I to VII, inclusive (Tr., 315-319), in favor of appellants.

9. The court erred in not finding and deciding that appellee herein has the legal right to divert from Rattlesnake Creek at the place designated on the maps introduced in evidence in this cause as "Dam" to the extent that it has need therefor, the water awarded and adjudicated to its predecessors in the decree in Cause No. 1953 by Rights Nos. 3, 8 and 14 of the Findings of Fact in said decree and within the limits and according to the priorities prescribed in said decree, for the purpose of supplying the city of Missoula and its inhabitants with water, but appellee does not have the right to divert at said place designated or said maps as "Dam" water to satisfy any of the other decreed rights included or adjudicated by the decree in Cause No. 1953 to its predecessors, whenever appellants have need for such water.

10. The court erred in not finding and deciding that the attempt by appellee and its predecessors in interest to change the place of diversion or Right No. 1 in the Findings of Fact in the decree in Cause No. 1953 from the head of the Mill ditch to the "Dam," and likewise the attempt of appellee and its prede-

cessors in interest, to change the place of diversion of Right No. 2, in the Findings of Fact of the decree in Cause No. 1953, from the head of original Higgins ditch to the "Dam"; and likewise the attempt of appellee and its predecessors in interest to change the place of appropriation of Right No. 9 in the Findings of Fact of the decree in Cause No. 1953 from the head of original Higgins ditch to the "Dam" are, and each of said attempts is, injurious to appellants, and said attempts cause, and each of said attempts causes, damage and prejudice to appellants and all of appellants.

11. The court erred in not finding and deciding that appellants are entitled to an injunction restraining appellee from making the changes in place of diversion of the water rights described in the complaint in this action and referred to in these findings, or making either or any of such changes, whenever appellant or any of appellants shall be unable to obtain water at his or their point of diversion on account of appellee's diversion, said appellant or appellants then having need for such water. Particularly appellants shall be entitled to enjoin and restrain appellee from changing the point of diversion of Right No. 1 of the Findings of Fact in the decree in Cause No. 1953 from the head of the Mill ditch to the "Dam" and shall be entitled to enjoin and restrain the appellee from changing the point of diversion of Right No. 2 of the Findings of Fact of the decree in Cause No. 1953 from the head of the original Higgins ditch to the "Dam," and

shall be entitled to enjoin and restrain appellee from changing the point of diversion of Right No. 9 of the Findings of Fact of the decree in Cause No. 1953 from the head of original Higgins ditch to the "Dam," at any time whenever appellants or any of appellants have need for the water to satisfy their own appropriations and are unable to obtain the water to satisfy their own appropriations because of appellee's diversion thereof.

12. The court erred in not finding and deciding the claim of appellee to have the right to change the point of diversion of the water awarded and decreed to its predecessors in interest in Findings 1, 2 and 9, from the head of the Mill ditch and original Higgins ditch to the "Dam," is wrongful and without authority of law and is invalid, being injurious to appellants, and appellee shall not have the right to make change of the point of diversion of said water rights, nor any thereof, whenever appellants, or any of appellants have need for such water and are deprived of the water on account of any diversion of water by appellee.

13. The court erred in not finding and deciding that the appellants were not guilty of laches, either in the commencement of their suit, or in the prosecution thereof, and that the appellants' right of action set forth in the pleadings herein against the appellee is not barred by laches.

14. The court erred in not finding and deciding that the appellants' action was instituted in good time and is not barred by the statute of limitations.

15. The court erred in not finding and deciding the issues herein in favor of appellants and against appellee.

There is appended to this brief the Statutes of Montana relating to water rights referred to herein.

VII.

ARGUMENT

SPECIFICATION OF ERRORS 8, 9, 10, 11, 12

Change of Point of Diversion

Section 7095, Revised Codes of Montana, 1921, gives to an appropriator the right to change the place of diversion *if others are not thereby injured*. If injury or prejudice result from the change of point of diversion, such change will not be permitted.

Maclay vs. Missoula Irrigation District, 90 Mont. 344, 3 Pac. (2d) 286, Para. X;

Cassard vs. Noies, 18 Mont. 216, 44 Pac. 959;

Head vs. Hale, 38 Mont. 302, 100 Pac. 222;

Carlson vs. City of Helena, 43 Mont. 1, 114 Pac. 110.

Unless sustained in law, the assertion by appellee of the right to change the point of diversion constitutes an infringement of the rights of appellants and justifies the issuance of an injunction.

Hanson vs. Larsen, 44 Mont. 350, 120 Pac. 229.

If not abandoned, and to the extent that the same are not abandoned, it may be conceded that decreed

Rights 1 and 2 are senior to any of the decreed rights of appellants. With the same qualification, it may be conceded that right 9 is superior to any decreed rights of appellants, except a portion of 5 owned by some of appellants. The pleadings and admissions of the parties and the uncontradicted evidence show that right 1 was appropriated and originally diverted from the stream through the Mill Ditch and Rights 2 and 9 were appropriated and originally diverted from the stream through the original Higgins Ditch and that these ditches tapped the creek at points below the several points of diversion of appellants; that long subsequent to the dates of the respective appropriations through the Mill Ditch and original Higgins Ditch, appellee and its predecessors abandoned both the Mill Ditch and original Higgins Ditch and assumed to change the place where the water for these appropriations was to be diverted to a point higher up on the stream and in the vicinity as the several places of diversion of appellants.

2nd. Some slight amount of testimony was offered tending to show a smaller volume than 1600 inches in some years in the fore part of August, the extreme low water period; likewise, some small amount of testimony tending to show that the creek at the street crossing above the head of the Mill Ditch, during the same period of the year, has been known to be dry. Little importance may be attached to this testimony; notwithstanding there may in the future come years of such drought that water will cease to rise in

the bed of the creek, and when the entire flow will be much less than the normal flow shown by the testimony, and yet, because such extreme conditions may be possible in widely separated years, perhaps once or twice in a lifetime, appellants are not to be denied relief for the greatly more numerous normal years to which they are entitled. Judging the future by the past, it is fair to estimate that for every drought year when the minimum flow will be less than 900 inches, there will be nine years when the minimum flow will approximate 1600 inches. During these normal years when the water flowing at the dam will approximate 1600 inches there will be sufficient to supply appellee's city water works appropriations of 705 inches, appellants' appropriations of 820 inches and a surplus going down the stream to add to the natural accretion so as to deliver water at the heads of the original Higgins Ditch and Mill Ditch to satisfy the earlier priorities of these ditches. We repeat, that this case should be decided upon the rights of the parties as such rights are likely to be determined by their conditions and their needs during the low water period of normal years. The likelihood that in the future years there may come such extreme droughts that no water will be available to satisfy appellants' appropriations ought not to prevent relief being extended to appellants for the greatly more numerous normal years when, if the water be distributed as provided by law, there will be sufficient to satisfy appellants' appropriations.

3rd. Appellee's counsel seem to suggest that the

amount of water rising in the bed of the stream above the head of the Mill Ditch and going to waste is only the amount measured in the weir. This measurement varied at different times from showing a depth of four inches on a ten foot weir to showing a depth of seven inches. A four inch depth of water on a ten foot weir measures 270, approximately, miners inches, while a seven inch depth figures 600 miners inches, approximately. To this amount should be added the flow in the Fredline Ditch running from 160 to 250 inches. This water in the Fredline Ditch, like the water in the creek bed, was all water rising below the dam and upon demand must be delivered into the Mill Ditch. That this water, in almost every year when anyone made observations, rose below the dam does not admit of argument. Engineers engaged by appellants measured it and appellants observed it; appellee's engineers observed and measured. That the measurements made by appellee's engineers were less than those made by appellants does not constitute proof of the incorrectness of appellants' measurements; it only shows that the amount varies at different times and under different conditions, but that *at times* the conditions pleaded by appellants actually exist and appellants' rights are to be fixed accordingly.

4th. Appellee's counsel suggest also that the right to make a change of point of diversion was acquired by the notice of appropriation, the record of which was offered in evidence, Ex. 13 (Tr., 243), and that in the decree in Cause No. 1953, the right to

change the point of diversion is expressly granted and recognized. These suggestions are not borne out by the record. Exhibit 13, which is record of water right notice and bears date July 26, 1887, shows that shortly prior to the date of the instrument Missoula Water Works and Milling Company made an appropriation of water for city water works purpose. In this document the appropriators refer to a prior appropriation of date November 16, 1868, and undoubtedly referring to Mill Ditch, Ex. 11 (Tr., 236), and an enlargement of that appropriation including perhaps original Higgins Ditch, which are referred to in Ex. 12. This latter appropriation also refers to a diversion originally made through the Higgins Ditch in 1871 for water right purposes. In the amended Complaint in Cause No. 1953, and upon which the case was tried, appellee's predecessor claimed various rights aggregating a total of 4200 inches from the years 1864 and 1868, the purposes of such appropriations being *for mechanical, agricultural, domestic and other useful and beneficial purposes*. The complaint seeks adjudication of plaintiffs' rights based upon these earlier appropriations, but suggest no change of point of diversion. To the amended complaint the several defendants answered denying the alleged appropriations and making issue thereof; these answers each, likewise, affirmatively alleged that the original appropriation of plaintiff, made for furnishing power for a grist mill (referring, no doubt, to the Mill Ditch) had been abandoned except for the use of 100 inches only. The

proof at this trial shows beyond argument that both the Mill Ditch and the Higgins Ditch were in actual use for not less than two years after the trial of Cause No. 1953. Upon these issues in Cause No. 1953, the court found as facts: (1) The appropriation of 946 inches, Mill Ditch, for mechanical, power, etc., purposes, the continuous use thereof to that time *and that no part thereof had ever been abandoned*; (2) and a like finding as to the Higgins Ditch appropriation; in fact, the water commissioner's report as late as 1906 shows distribution by the water commissioner of the Higgins Ditch appropriation to the Higgins Ditch and its use for agricultural purposes and the payment of the water commissioner's assessment by the ditch owner for the water distributed for the purpose; (3) an appropriation of 13½ inches for city water works purposes April 1, 1871; an enlargement thereof April 1, 1881, for city water works purposes 60 inches; and, No. 14, further new construction and appropriation for the same purpose, 645 inches June 1, 1887. Thus by every reasonable, fair intendment, the decree found upon the issues presented and the result is clear that no right was given to appellee's predecessors to change either the Mill Ditch or the Higgins Ditch appropriation to divert the same higher up upon the stream, the proof being clear that when Cause No. 1953 was upon trial in 1902 there was the water actually flowing to satisfy the appropriations in both Mill Ditch and Higgins Ditch. The expressed finding against the abandonment of such appropriation was sustained. Likewise, the court in Cause No. 1953 cannot be deemed

to have decreed or granted a change in place of diversion when at the very time of the trial of No. 1953 the water was still being diverted at the point of original appropriation. On the other hand, the various appropriations by the predecessors of the plaintiffs in Cause No. 1953 are readily reconciled with the court's findings in Cause No. 1953. We know that claims to water in water right suits invariably greatly exceed awards of water decreed. Exaggerated demands are invariably expected but the awards made are based upon the testimony and not upon the demands. So when plaintiff in Cause No. 1953 was awarded Right 1, 2 and 9 for the Mill and Higgins Ditch, we must indulge the presumption that these appropriations in the amounts awarded were sustained by testimony. Likewise, awards of 131½ inches No. 3, 461½ inches No. 8, and 645 inches No. 14 for city water works purposes must be assumed to be in accord with the testimony produced. If it had been the fact that at the time of such trial the Mill Ditch appropriations were then being diverted at the dam the court would not have awarded 945 inches for the Mill Ditch and would not have further found *that no part thereof has ever been abandoned*.

5th. The diversion at the dam and additional works there constructed and referred to in the notice of water right, Ex. 13, even though taking water formerly diverted through the Mill Ditch, constituted a new appropriation of the date of the new construction.

Featherman, et al. vs. Hennessy, et al., 43 Mont. 310, 115 Pac. 985.

The court in Cause No. 1953 manifestly so concluded and gave the appropriator 645 inches of date June 1st, 1887, for city water works purposes, Right 14. The diversion for city water works purposes made in the year 1871 and referred to in the notice of location, Ex. 12, and the additions and enlargements thereof, likewise referred to in Ex. 12, were not disregarded by the court in the trial of Cause No. 1953 but Rights No. 3 and 8 were given on account thereof. The suggestion is made that by the statute of 1885 the right to change the point of diversion is given, but the Section in question, being Section 1251, Page 995, Compiled Statutes of Montana, 1887, is identical with the statute now and referred to by the Supreme Court of this state. In effect, the point of diversion may be changed *if others are not thereby injured*, but when the change causes injury to another then, as stated in Featherman vs. Hennessy above, it constitutes a new appropriation. Thus it is apparent that all the issues presented to the court in Cause No. 1953, and while exaggerated claims were cut, as they should have been, to conform to the needs of the appropriators, still rights were granted for all appropriations of which we now have knowledge. In the absence of any record whatever to bear out the claim, this court ought not to be asked now to assume, a wholly speculative assumption, that other issues were passed upon and other rights extended not apparent in the decree in Cause No. 1953, Sloan vs. Buyers, 37 Mont. 503, where the

court, quoting with approval from the Supreme Court of New Jersey, says:

“Persons by becoming suitors do not place themselves for all purposes under the control of the court, and it is only over these particular interests which they choose to draw in question that a power of judicial decision arises. . . .

“A judgment upon a matter outside of the issue must of necessity be altogether arbitrary and unjust, as it includes a point upon which the parties have not been heard. And it is upon this very ground that the parties have been heard, or have had the opportunity of a hearing, that the law given so conclusive an effect to matters adjudicated. And this is the principal reason why judgments are not estoppels. But records or judgments are not estoppels with reference to every matter contained in them. They have such efficacy only with respect to the substance of the controversy and its essential concomitants.”

Freeman on Judgments, 5th Edition, Volume I, Section 76:

“It is always proper to consider what the judgment should have been, since it will be ‘presumed that the court intended to adjudge correctly in law upon the facts of the case,’ and of two possible interpretations of the language of the judgment, that one will be adopted which makes it correct and valid, in preference to one which would make it erroneous.”

Gans and Klein Investment Company vs. Sanford, 91 Mont. 512:

“As with other documents, the legal operation and effect of a judgment must be ascertained by

construction and interpretation of it. The legal effect is that which governs. Judgments are to have a reasonable intendment; where a judgment is susceptible of two interpretations the one will be adopted which renders it the more reasonably effective and conclusive and which makes the judgment harmonize with the facts and law of the case.

“A decree will not be construed so as to result in positive wrong where that result can possibly be avoided.”

21 Corpus Juris, Page 689:

“A decree will not be construed so as to result in a positive wrong where that result can possibly be avoided.”

For appellee to ask this court to find that it was awarded the right in Cause No. 1953 to change the point of diversion of the Mills and Higgins Ditch appropriations is not only contrary to the positive rights extended to those ditches on account of water actually flowing in those ditches at the very time Cause No. 1953 was upon trial, but is also contrary to the express provision of Section 10561, which provides:

“That only is deemed to have been adjudged in a former judgment which appears upon its face to have been so adjudged, or which was actually and necessarily included therein or necessary thereto.”

The appellee introduced in evidence the proceedings in the Kemp condemnation suit (Tr., 271). We assume this evidence was offered for the purpose of tending to show that prior to the trial of Cause No.

1953, appellee intended to and was preparing to change its place of diversion from where it had been near the Feddersohn barn yard to a point higher up on the stream and where the present dam is situated.

Appellee's testimony very clearly showed that this change of place of diversion was made principally, if not solely, to avoid the contamination of its water by refuse from the Feddersohn cow yard. Appellee's evidence indicated clearly that in the spring time, especially, refuse from the cow barn yard would seep into the water and be carried to the reservoir.

There was nothing in this change of place of diversion which could or would in any manner lead the appellants' predecessors to believe that the appellee's predecessors contemplated using the water of the Mill ditch or Higgins ditch at the new dam. This change was entirely consistent with the idea that the water company, desiring to avoid the contamination of refuse from the barn yard, decided to change the place of diversion of its rights Nos. 3, 8 and 14 to the place where it constructed its new dam, being the place where the present dam is situated.

It will, of course, be borne in mind that neither Kemp nor his successors were parties to this action.

We believe that it very clearly appears that at the time of the signing of the decree in Cause No. 1953, water was being used by the appellee's predecessors through both the Mill Ditch and Higgins Ditch. The decree expressly finds that no part of the water decreed to these ditches had been abandoned. Any change in

the place of diversion *or any change of the use* of the water in either ditch would of necessity result in injury and prejudice to the predecessors of appellants in this action.

The language of the Supreme Court of Montana in the case of Galiger vs. McHulty, 80 Mont. 339, 260 Pac. 401, is very pertinent in these circumstances. The court said on page 357:

“It is settled law in this state that an appropriator may change the place of diversion and change the use of the water (Thomas v. Ball, 66 Mont. 161, 213 Pac. 597), but such a change cannot be made to the prejudice of subsequent appropriators (Head v. Hale, 38 Mont. 302, 100 Pac. 222; Carlson v. City of Helena, *supra*; Lokowich v. City of Helena, *supra*). But an appropriator cannot be permitted to use the water for the purpose for which it is appropriated, and then, in the interims when not continually used by him, sell the same for use by other persons. The supreme court of Montana, in considering this question, used this language: ‘It has been held that an appropriator of water may change the use of his appropriation from one purpose to another, (Meagher v. Hardenbrook, 11 Mont. (385) 381, 28 Pac. 451, and cases cited), but it has never been held in this state (nor are we cited to like holding elsewhere) that after an appropriator has used the water sufficiently to answer the purpose of his appropriation, he might take the waters of the stream remaining, which he could not use for the purpose of his appropriation, and sell it to other parties, thereby depriving subsequent appropriators of their right to use the same.’ (Creek v. Bozeman Waterworks Co., 15 Mont. 121, 131, 38 Pac. 459; see, also Tucker v. Missoula Light & Water Co., 77 Mont. 91, 250 Pac. 11.)”

SPECIFICATION OF ERRORS 13, 14

Adverse Possession and Laches

6. Appellants respectfully urge that the pleading in this case falls far short of showing that appellants' right is barred by any limitations of the statutes or by laches. Likewise, the testimony wholly fails to support any such claims. We invite the court's attention to the case of:

Zosel vs. Kohrs, 72 Mont. 564, 234 Pac. 1089, cited with approval in St. Onge et al. vs. Blakely, 76 Mont. 1. The Supreme Court of Montana in the Zosel case lays it down as a fundamental rule that a decreed user from an adjudicated stream, such as appellee here, will be presumed to be taking water which it diverts pursuant to the decree, unless and until such user repudiates the decree and expressly gives notice to other users of such repudiation. To constitute a sufficient pleading of right by prescription it is incumbent upon the pleader to show a taking of the water when the rightful owner has need for it; and invasion of the right of the true owner. In case the true owner, at the time of such invasion, would not have need for the water, then there would be no actual invasion of his right and no initiation of the statute of limitations, "and it is only when it becomes so scarce that all of the parties cannot be supplied that an appropriator by taking that which by priority belongs to another can be said to initiate an adverse use." To establish a right by adverse possession the pleader must show

“that during the entire statutory period her invasion of the rights of the defendant were such as to give them, or some of them, a cause of action against her.”

Citing:

Smith vs. Duff, 39 Mont. 374;

Chessman vs. Hale, 31 Mont. 577;

Boehler vs. Boyer, 72 Mont. 472;

Talbott vs. Butte City Water Company, 29 Mont. 17;

Norman vs. Corbley, 32 Mont. 195.

He who asserts right by adverse possession has the burden of pleading and proving such right.

Stagg vs. Stagg, 90 Mont. 180.

7. In the light of these well-established rules, let us briefly analyze the situation as disclosed by the testimony in this case. Appellee had been decreed 60 inches of water for city water works purposes by Rights Nos. 3 and 8 in Cause No. 1953 and an additional 645 inches for the same purposes by Right No. 14. For each of these appropriations it fairly appears that the appropriator constructed substantial improvements upon the stream by which to divert and use the appropriation. Nobody claims and nobody has pleaded nor testified that the water of the creek ever reached so low a stage as to cut off Right No. 14 nor any part of it, nor any prior right. It seems, in fact, conclusively established that with the possible exception of two or three very brief periods there has al-

ways been sufficient water to supply Right No. 14 and prior rights throughout the entire history of the Rattlesnake. All users under decree were warranted in assuming that all appropriators *in taking the water from the streams, did so pursuant to the provisions of the decree*, Zosel vs. Kohrs, supra; also it is true that the presumption will be indulged that appellee and its predecessors did not intend to violate the decree, but it seems fairly apparent in this case that appellee and its predecessors did not violate the decree, but on the other hand, appellants and their predecessors received the water awarded to them, respectively, by the decree. From the time of the decree to the year 1931, with only slight interruptions, the appellants and their predecessors lived upon their farms, irrigated extensively, developed their lands and grew crops in abundance. From the unimproved area found by the first settlers, the locality has been developed by the use of the water of Rattlesnake Creek in the irrigation of the lands, to a settled, highly improved, prosperous community. This negatives the thought of an adverse use for city water works purposes of Rattlesnake Creek flow. No witness negatived such use of the water for irrigation although annoying encroachments, no doubt, occurred; all agree that in 1931 the previous vague assertions of right by appellee became outspoken proclamations. For the first time appellants then were made aware of the adverse claims, appellee then took the entire flow of the stream with the result of a complete loss of crops to appellants. Then for the first time, no

doubt, the right to bring this action became apparent. Under such circumstances, there is little foundation for the claim that appellants' action is barred by the statute of limitations.

8. The answer pleads that appellants' cause of action is barred by Section 9041, which provides a limitation of five years. This section is one intended to cover cases not particularly provided for by previous statutes. Appellee pleads no other statute of limitation. But a water right is real property, and an adverse title thereto could not be established short of the ten year period prescribed by Section 9015.

Boehler vs. Boyer, 72 Mont. 472, 234 Pac. 1986;

Wiel on Water Rights, Vol. 1, Sec. 583;

Smith vs. Duff, 39 Mont. 374, 102 Pac. 981.

The open, notorious, exclusive, uninterrupted use of water under claim of right is not sufficient to constitute an adverse user unless it is shown that the one against whom the adverse claim is asserted had need for the water and was actually deprived thereof.

In the case of Smith vs. Duff, 39 Mont. 374, the court said on page 378:

“Because of the nature of the right, the elements constituting it must be proven satisfactorily and unequivocally; and no doubtful inference will suffice. The right by adverse user, or prescription, is acquired, in some measure, by an invasion of the rights of others—it bears a sort of kinship, by refined descent to the ‘possession by bow and spear’ of an earlier time; it is based upon a posi-

tive assertion of right in and by the water user in derogation of the rights of everyone else. In order to constitute an ownership by adverse user, say the authorities, the use must have been open, notorious, continuous, adverse and exclusive under a claim of right for the statutory period, which in this state is now ten years. (See *Talbott v. Butte City Water Co.*, 29 Mont. 17, 73 Pac. 1111, and authorities cited.) While the authorities use both the words 'open' and 'notorious,' the use of either would seem to be sufficient, as they are practically synonymous when used in this connection, as inspection of the dictionaries will show. We advert to this because of the contention of counsel respecting the pleadings. Because of the conclusion to which we have come, we do not make further mention of the pleadings.

It is essential that the use be shown to have been adverse. Proof of the mere use of the water during the statutory period is not sufficient. It is necessary that during the entire period an action could have been maintained against the party claiming the water by adverse user by the party against whom the claim is made. (*Talbott v. Butte City Water Co.*, *supra*; *Chessman v. Hale*, 31 Mont. 577, 79 Pac. 254, 68 L.R.A. 410; *Norman v. Corbley*, 32 Mont. 195, 79 Pac. 1059; *Watts v. Spencer*, 51 Or. 262, 94 Pac. 39.) In the case last cited, *Watts v. Spencer*, the supreme court of Oregon said: 'The acts by which it is sought to establish the prescriptive right must be such as to operate as an invasion of the right of the person against whom the prescriptive right is asserted, and will give cause of action in his favor. (Long on Irrigation, sec. 90.) No adverse user can be initiated until the owners of the superior right are deprived of the benefit of its use in such a substantial manner as to notify them that their rights are being invaded. (*Wimer v. Simmons*, 27 Or.

1, 50 Am. St. Rep. 685, 39 Pac. 6; North Powder Co. v. Coughanour, 34 Or. 9, 54 Pac. 223; Bowman v. Bowman, 35 Or. 279, 57 Pac. 546; Boyce v. Cupper, 37 Or. 256, 61 Pac. 642.)' See also, Bullerdick v. Hermsmeyer, 32 Mont. 541, 81 Pac. 334."

9. In the same manner, why should appellee be permitted to assert that appellants are guilty of laches? The rule is stated in 21 C. J. 221, Par. 219, as follows:

"But mere delay in asserting a right does not *ipso facto* bar its enforcement in equity, by the great weight of authority, unless the case is barred by the statute of limitations. To constitute a defense, the delay must have been such as practically to preclude the court from arriving at a safe conclusion as to the truth of the matters in controversy, and thus make the doing of equity either doubtful or impossible, as through loss or obscuration of evidence of the transaction in issue, or there must have occurred in the meantime a change in conditions that would render it inequitable to enforce the right asserted, or, as commonly phrased, the delay must have worked injury, prejudice or disadvantage to defendant or others adversely interested, or plaintiff must have abandoned or waived his right, or acquiesced in the assertion or operation of the adverse right, or lost his own right by estoppel, or sufficient time must have elapsed to create or justify a presumption against the existence or validity of plaintiff's right, or a presumption that if plaintiff was ever possessed of a right, it has been abandoned or waived or has been satisfied, or that in consequence of the delay the adverse party would be inequitably prejudiced by the enforcement of the right asserted."

And in the First State Bank vs. Mussigbrod, 83

Mont. 68, 271 Pac. 695, the court, at page 89, spoke of the rule regarding laches, as follows:

“Plaintiff assigns error on the court’s finding that the interveners were not guilty of laches in asserting their rights, and contends that evidence warrants a finding of laches barring recovery.

Plaintiff relies chiefly upon the declarations of this court found in *Riley v. Blacker*, 51 Mont. 364, 152 Pac. 758, that ‘laches means negligence in the assertion of a right; good faith and reasonable diligence only can call into activity the powers of a court of equity, and, independently of the period fixed by the statute of limitations, stale demands will not be entertained or relief granted to one who has slept upon his rights. Considerations of public policy and the difficulty of doing justice between the parties are sufficient to warrant a court of equity in refusing to institute an investigation where the lapse of time in the assertion of the claim is such as to show inexcusable neglect on the part of the plaintiff, no matter how apparently just his claim may be; and this is particularly so where the relations of the parties have been materially changed, etc.’ It never has been questioned, to our knowledge, that the death of one of the parties to the transaction is such a change.”

And again:

“Although a court of equity will not enforce a resulting trust after a great lapse of time, or laches on the part of the supposed *cestui que* trust, when the trust is admitted and there has been no adverse holding, lapse of time is no bar; ‘any excuse for delay which takes hold of the conscience of the chancellor and makes it inequitable to interpose the bar is sufficient.’ ”

Laches cannot be presumed from delay alone. In *Cox vs. Hall*, 54 Mont. 154, 168 Pac. 519, the court said, on page 164:

“We have repeatedly declared that though ‘laches may arise from an unexplained delay short of the period fixed by the statute of limitations . . . still laches will not be presumed from such a delay alone. It must be made to appear affirmatively that unusual circumstances exist which on account of such delay render the proceeding inequitable; else relief cannot be denied on this ground.’ (*Brundy v. Canby*, *supra*; *Wright v. Brooks*, 47 Mont. 99, 130 Pac. 968.) No such circumstances are presented here.”

And in the case of *Parchen vs. Chessman*, 49 Mont. 326, 143 Pac. 631, at page 340:

“Since it had been in the possession of the plaintiff, and had not been seen by the defendant, the latter could have had no knowledge that the mistake had been made until he ascertained the fact from the copy of the complaint served upon him. *Prima facie* this was sufficient to excuse his delay, for he was not required to act until he discovered that a mistake had been made. In any event mere delay is not sufficient ground for the imputation of laches. (*Wright v. Brooks*, 47 Mont. 99, 130 Pac. 968.)”

We call the court’s attention to the statement of the rule as applied to laches in Montana, as set forth in the case of *Hynes vs. Silver Prince Mining Company*, 86 Mont. 10, 281 Pac. 548, at page 16, as follows:

“‘Laches’ has been defined as ‘Such neglect or omission to assert a right as, taken in conjunction with the lapse of time, more or less great, and

other circumstances causing prejudice to an adverse party, operates as a bar in a court of equity.' (10 Cal. Jur. 520.) Considered as a bar, independent of the statute of limitations laches means negligence in the assertion of a right; it is the practical application of the equitable maxim 'equity aids the vigilant,' and it exists when there has been unexplained delay of such duration or character as to render the enforcement of the asserted right inequitable. (Riley v. Blacker, 51 Mont. 364, 152 Pac. 758.) It has been a recognized doctrine in courts of equity, from the very beginning of their jurisdiction, to withhold relief from those who have delayed for an unreasonable length of time in asserting their claims. The doctrine of laches is based upon grounds of public policy which requires, for the peace of society, the discouragement of stale demands. And where the difficulty of doing entire justice by reason of the death of the principal witnesses, or because, if living, the facts relating to the original transaction have faded from their memory or become obscured by lapse of time, is attributable to gross negligence or deliberate delay, a court of equity will not aid a party whose application is destitute of good faith, conscience and reasonable diligence."

The Supreme Court of the United States recognizes principle in the case of Hammond vs. Hopkins, 143 U. S. 224, 36 L. Ed. 134, 12 Sup. Ct. Rep. 418:

" 'That a court of equity will not aid' a party whose application is destitute of conscience, good faith and reasonable diligence."

We think it cannot be successfully urged here that the plaintiffs' application lacks either conscience, good faith or reasonable diligence.

10. Applying these well established rules to this case, the appellants knew that appellee's predecessors were furnishing water to the city of Missoula and its inhabitants and that the right to use the water of Rattlesnake Creek for such purpose was expressly decreed in Findings of Fact Nos. 3, 8, and 14, aggregating 705 miners inches. From the testimony it would seem that 700 inches were perhaps the maximum required for appellee's purposes until very recent years. The witness T. T. McLeod described the use for city purposes in the years immediately following the trial of Cause 1953, and down to about 1907 at less than 400 inches (Tr., 203). It is safe to assert that prior to 1908 the maximum flow was less than 400 inches. The improvements and the large expenditures of money made by appellee's predecessors for the enjoyment of their water rights were made during T. T. McLeod's management of the property. Having decreed rights for city water works purposes for more than 700 inches, greatly in excess of the maximum used, might it not be fairly presumed by the other appropriators that the improvements and expenditures in question were made with the intention of the water company to use its decreed rights, and to use the appropriations which it had been decreed for the purpose which it had the right to use them? Were other appropriators to presume that the water company would allow the rights decreed for water works purpose to go to waste and an unlawful use made of another right? We earnestly urge that the water company must be presumed to have

made the expenditures and improvements referred to with the intention of using the water rights which it had the right to use, and without the intention to trespass upon the rights of the appellants. Accordingly and for many years after that time, the predecessors of these appellants enjoyed their decreed water as distributed by the water commissioner. They cultivated their lands, irrigated their crops and, generally speaking, were prosperous. Prior to 1931 (except in the case of Tucker for which appropriate compensation was paid) appellee's predecessors seemed not guilty of excessive invasion of the rights of appellants' predecessors. In fact, under the rule in *Zosel vs. Kohrs*, a cause of action did not accrue prior to 1931.

11. Furthermore, it is not claimed, neither pleaded nor proven, that the operation of its water rights by defendants' predecessors has not always been highly profitable and enjoyable. It is not claimed that the improvements made and expenditures of money were on account of the expectation of being permitted to change the place of diversion of Rights 1, 2 and 9. The fair inference is that the expenditures and improvements made, were made because of the right, undisputed, to use water rights 3, 8 and 14 for water works purpose. There is not a particle of testimony to indicate that appellee's predecessors ever actually needed to divert rights 1, 2 and 9 at the "Dam" in order to sufficiently supply Missoula and its inhabitants with water.

Furthermore, there is no serious claim that ap-

pellee will not use and enjoy its improvements and water works enterprise to the fullest extent by receiving its Rights 3, 8 and 14. This case fails to show any need of defendant to divert any part of right 1, 2, or 9 at the "Dam." In fact the fair inference from the testimony is positive that Rights 3, 8 and 14 at the "Dam" are ample for its needs.

In deciding the case in the court below, the Honorable Judge makes no reference to the pretended defenses of laches, or that appellants' rights may be barred by the running of any statute of limitations; the Honorable Judge expressly states, however, that he ignores *nonessentials of strategy, camouflage, and nuisance-value*, and we may assume that these so-called defenses are included in this category and merit no mention. The same are discussed in this brief in anticipation of appellee's claims in respect thereto but in view of the same being eliminated by the court below, we feel that the discussion is not important and that further discussion of the subjects is unnecessary.

SPECIFICATION OF ERRORS 1, 2, 3, 4

12th. The Honorable Judge of the court below found no difficulty in determining the facts in this case in favor of appellants in their claim that appellee had transgressed the privilege extending by Section 7095, and that appellants are prejudiced by the attempted change of point of diversion; appellants' grievance is expressed as *clear, plain as a pike staff*. The court below calls attention to the fact that the

decree of 1903 was a decree of the state court and enjoins all parties from transgressing upon the rights of all others. The state court retains jurisdiction to enforce the decree, apportion the water and supervise its use by its officer (water commissioner).

From that the court decides that any trespasses upon, or violation of, the rights involved must forever remain a subject of jurisdiction by the state court. The important question to be determined in this appeal is the correctness of this holding in the trial court.

Article III of the Constitution of the United States provides that the judicial power of the United States shall extend to all cases in *law and equity arising between citizens of different states*. The necessary diversity of citizenship and value in controversy is alleged and admitted (Tr., 3, para. I; Tr., 60, para. I). The constitutional provision is carried out by USCA Title 28, Section 41. Thus, unless precluded by the fact that the state court adjudicated the extent and priority of the appropriations of the several users and that the state court continues by its officer (water commissioner), to apportion the water each year and, to some extent, supervise its use, then appellants have clearly shown their right to have this court take heed of their complaint and grievance.

A water right in Montana is a form of property recognized by the laws of the state.

Section 7093, Rev. C. 1921;

Wiel on Water Rights, Chap. 2, Page 14;

Toohey vs. Campbell, 24 Mont. 13, 60 Pac. 396;

Conrow vs. Huffine et al., 48 Mont. 437, 138 Pac. 1094;

Thorpe vs. Freed, 1 Mont. 651;

Mettler vs. Aimes Realty Co., 61 Mont. 152, 201 Pac. 702;

Smith vs. Denniff, 24 Mont. 20, 60 Pac. 398;

Moore vs. Sherman, 52 Mont. 542, 159 Pac. 966.

“The right acquired by Miller by virtue of his appropriation in 1892 was property. It continued to be property to the time of his death and passed to his successors.”

Such property right has its inception in the making of a valid appropriation in form prescribed by law, Section 7094, Rev. C. 1921, *Bailey vs. Tintinger*, 45 Mont. 154, 122 Pac. 575. The rule is that first in time is first in right, Section 7098, Rev. C. 1921. The property right originates because of the appropriation and not by virtue of the decree.

Bennett vs. Quinlan, 47 Mont. 247, 131 Pac. 1067;

Whitcomb vs. Murphy, 94 Mont. 562, 23 Pac. (2nd) 980.

An adjudication such as was accomplished in Cause No. 1953 is intended only and has the effect only of prescribing and defining the rights actually acquired by the appropriator by virtue of his appropriation, and the relationship of such rights to one another, Section 7105, Rev. C. 1921.

13th. It is true that the court, by virtue of the statute, retains, in a sense, authority over the area and water flowing, by its officer (water commissioner) for the distribution of the water. Section 7136, Rev. C. 1921 to 7159 inc., amended by Chapter 125 of the 19th session, 1925. But the duties of the water commissioner are purely ministerial and in no sense judicial.

Gans and Klein Invest. Co. vs. Sanford, et al.,
91 Mont. 512, 2 Pac. (2nd) 808.

This action involved a complaint of the distribution made by the water commissioner under Section 7150 as amended by Chapter 125, Laws of 1925. The court say:

“The only pleading required by section 7150, as amended, *supra*, is the written complaint of a water user who is dissatisfied with the manner in which the commissioner is distributing the water. The method prescribed is a simple one: A person deeming himself injured by the actions of the commissioner lodges with the judge (or files with the clerk) a written complaint, upon which the judge fixes a time for hearing, directing that ‘such notice be given to the parties interested in such hearing as the judge may deem necessary.’ At the time fixed the judge hears and examines the complainant and such other parties as may appear to support or resist the claim, as well as the water commissioner and other witnesses as to the charges contained in the complaint. The sole question for determination is whether the water commissioner has been distributing the water to the respective users in accordance with the decree. It is possible that in time of low water the judge

may be obliged to hear a number of complaints under this section of the statute during an irrigation season. The statute does not contemplate that a formal trial framed upon pleadings filed by the respective parties, shall result from the mere filing of a complaint. Supposedly when a water right suit ends in a final decree, all of the issues contemplated therein are adjudicated. The decree is not merely a basis for a new procession of water suits. In the administration of the decree it may happen for one reason or another that the water commissioner may need directions from the judge respecting the distribution of the water."

In practice, that we must all be aware that the water commissioner (commonly designated as ditch tender) is not a person learned in the rules covering the ownership and rights to property, nor skilled in deciding upon such rights. Generally speaking, he is of the unfortunate type who is favored with a passing job because he has neither the physical nor mental ability to retain steady work. It is not to be considered for a minute that the decision of so important a question as, for instance, the right to change the point of diversion of the appropriation, such as is claimed by appellee for the Mill Ditch, or either the Higgins Ditch, must first be made by the water commissioner. To suggest the submission of so important a matter to the water commissioner for decision is only making ridiculous the administration of law. Clearly, the water commissioner's function is to distribute the flow of the stream in the amount and of the priority outlined in the decree, any changes that may occur in the

volume of the flow, the place of diversion, the necessities of the appropriators and similar questions are the subject of judicial inquiry to be determined by the courts and not to be decided in the first instance by the water commissioner.

Boulder & Left Hand Ditch Co. vs. Hoover
Water Commissioner (Col.), 110 Pac. 75.

holds duties of water commissioner ministerial, not judicial:

“never was in contemplation that they should examine the burden of litigation because of dispute between the several water claimants, with reference to their respective rights under decrees duly rendered and enforced.” “If plaintiff, when the water is turned out to him makes an improper use thereof applying it unlawfully to another land, or otherwise wrongfully uses it, in a way to injure the fixed rights of others interested in the same source of supply, then such wrong is subject to correction *in a suit by the one damnified.*”

Rosenkrantz vs. Barde (Ore.), 214 Pac. 889;
Parchall vs. Cooper, 22 Wyo. 385, 134 Pac.
302.

“by, not exercising that duty, (referring to distribution of water as water commissioner) *he has no authority to determine whether or not a water right has been forfeited or amended, or to prevent an appropriator from taking the full quantity of water awarded by the board of control.*”

In 40 Cyc. 730, the rule is stated that a court of equity may adjudicate and determine the extent of

rights in water flowing in natural streams and to regulate the use of the flow by the appropriator and the jurisdiction of the Federal Court is recognized where requisite diversity of citizenship exists. Injunction proper remedy, 40 Cyc. 738. Assertion of adverse claim sufficient to justify quiet title, 40 Cyc. 729.

Without discussion the court upheld right to maintain suit such as this in:

Thrasher vs. Mannix & Wilson (Mont.), 26 Pac. (2nd) 370,
and in Donich vs. Johnson, 77 Mont. 229, 250 Pac 963,
where a suit for permission to establish reservoir site on stream entertained.

Bennett vs. Quinlan, 47 Mont. 247, 131 Pac. 1067:

“As appears from the foregoing statement, it is alleged therein that the plaintiff is the owner of the property described, that defendant claims an interest therein adverse to that of plaintiff, and that such claim is without right. This is sufficient to put the defendant upon his defense. (Mont. Ore Pur. Co. v. Boston & Mont. C. etc. Co., 27 Mont. 288, 70 Pac. 1114; Merk v. Bowery Min. Co., 31 Mont. 298, 78 Pac. 519; Castro v. Barry, 79 Cal. 443.)”

14th. Wherever the question has arisen the courts (including Montana) have uniformly held that the right to the use of water flowing in a stream acquired by virtue of an appropriation is of such dignity and importance that in case of trespass upon it, or transgression against it, the owner of the right is not limited in his remedy to first appealing to a water commissioner but may appeal to any court of competent

jurisdiction, the same as he might do for the protection, or preservation, of any other property or personal rights. In providing for a water commissioner to distribute the water of an adjudicated stream and in permitting a complaint to be made for his wrongful distribution, it was intended to provide *an additional remedy, not an exclusive remedy*. And it is expressly held that the property owner, at his election, may enter a court of competent jurisdiction and seek and obtain the necessary protection of his right and the courts will entertain such a suit.

Tucker vs. Missoula L. & R. Co., 77 Mont. 91, 250 Pac 11;

Buskirk vs. Red Butte Co., 24 Wyo. 183, 156 Pac. 1122, 160 Pac. 387.

Appellants' Brief, same case, page 64, citing:

Allen vs. Houn (Wyo.), 219 Pac. 573, para. 9;

Maize vs. Dist. Court for Butte County, Idaho, 200 Pac. 115.

15th. Apply the foregoing principles to the situation now before the court. In litigation commenced in 1901 in the Montana Court, having jurisdiction of the res, a decree was rendered in 1903. The amounts and relative priorities of all appropriations from Rattlesnake Creek were adjudicated. The plaintiff in that action, appellee's predecessor, claimed large appropriations aggregating 4200 inches for *mechanical, agricultural, domestic* and other useful and beneficial purposes but not alleging any change of point of di-

version nor asking permission to make such change. Upon issue formed by the various answers and upon evidence given upon trial the court found as fact that plaintiff's predecessors had appropriated, (a), 946 inches for mechanical power and other purposes by the Mill ditch, (b), 160 inches by the Higgins ditch, and, (c), 348 inches more by the Higgins ditch. There is no pleading whereby the court would have had the right to pass upon the question of a change of point of diversion nor is there any suggestion that the court did actually attempt to nor give any right to change the point of diversion. In 1931 the previous doubtful rumblings of such an intention became an open declaration that appellee had changed the point of diversion of Mill ditch and Higgins ditch appropriations to the "Dam" and thenceforth and regardless of the effect such transfer might have upon the appropriations of appellants, it proposed to divert these appropriations at the "Dam." As is stated by the Honorable Judge who tried the cause, appellants thereby are justified in complaining, their grievance and injury is real and substantial which result is *plain as a pike staff*. The prescribed amount in controversy and diversity of citizenship being present, are the doors of the courts of the United States closed to appellants in which they may complain of the injury thus inflicted upon them? The Honorable Judge of the court below, without suggestion from counsel for appellee and without argument nor reference to authority, so decided. The decisions referred to by him do not sustain the view ex-

pressed, nor can authorities be found that will sustain such view.

The rule is that a federal court may not take jurisdiction because the same litigation is pending in a state court applies only where the parties to, the subject-matter of, and the relief sought in the suit in the federal court are identical with that in the state court.

15 C. J. 1163, para. 638.

Buck vs. Colbath, 3 Wall (U. S.) 334, 18 L. Ed. 257:

“It is not true that a court, having obtained jurisdiction of a subject-matter of a suit, and of parties before it, thereby excludes all other courts from the right to adjudicate upon other matters having a very close connection with those before the first court, and, in some instances, requiring the decision of the same questions exactly. In examining into the exclusive character of the jurisdiction of such cases, we must have regard to the nature of the remedies, the character of the relief sought, and the identity of the parties in the different suits.”

Appellants here are successors of some, but not all, of defendants in Cause No. 1953. They join here in asking relief against appellee's encroachment but their joining is a mere incident, any one of them would have had the right to maintain the action alone. Such being the case, it can scarcely be asserted that there is an identity of parties in this action with the parties in Cause No. 1953. Likewise, the relief sought is wholly different in this case than it was in the former

case. That case was strictly an adjudication of the stream to determine relative priorities and amounts of appropriations; this case is to restrain an encroachment upon appellant's rights by changing the point of diversion. The reference, in this case, to the water rights of the various parties by the decreed number is likewise merely incidental and a matter of convenience. All such rights, as we have seen, were initiated by appropriation and not by the decree and our reference to them by decree number is only because of the convenience of so doing.

Knuth vs. Lepp (Wis.), 193 N. W. 519;

Lippke vs. Portable Milling Co. (Ia.), 244 N. W. 845;

C. T. C. Invest. Co. vs. Daniel Boone Coal Corporation, 58 Fed. (2d) 305;

Carter vs. Blaine Co. Invest. Co., 45 Fed. (2d) 643;

Hunt vs. New York Cotton Exchange, 27 Sup. Ct. Rep. 529;

Ingersoll as admx. vs. Coram, 29 Sup. Ct. Rep. 92;

Watson vs. Jones, 13 Wall 679, 20 L. Ed. 666.

“But when the pendency of such a suit is set up to defeat another, the case must be the same. There must be the same parties or, at least, such as represent the same interest, there must be the same rights asserted, and the same relief prayed for. This relief must be founded on the same facts, and the title or essential basis of the relief

sought must be the same. The identity in these particulars should be such that if the pending case had already been disposed of, it could be pleaded in bar as a former adjudication of the same matter between the same parties.”

The case of *Pacific Livestock Co. vs. Lewis, et al.*, 36 Sup. Ct. Rep. 637, seems to be on all fours with the present case. In that case, the purpose and effect of an adjudication of water rights is reviewed and defined. The distinction between such an adjudication and a case such as this is pointed out. The opinion in that case by Justice Van Devanter seems unanswerable and clearly holds that the United States Court, under the circumstances, should not dismiss a case such as this but should decide the same upon the merits.

SPECIFICATION OF ERRORS 5, 6, 7

16th. The discussion foregoing covers anything that might be said as to these specifications of error and the same are submitted without further reference.

FINAL DISPOSITION OF THE CASE

17th. Having shown that the court below, after clearly deciding the matters in issue in favor of appellants, denied them relief because of the erroneous belief that the court should not entertain the complaint, the question presents itself as to the disposition that now should be made of the case. Being an equity suit,

the whole case is before the court and the same should be decided *de novo* on its merits.

Wong Keow vs. U. S., 215 Fed. 95;
Waterloo Min. Co. vs. Doe, et al., 82 Fed. 41;
Unkle vs. Wills, 281 Fed. 29, 34;
Idaho M. & M. Co. vs. Davis, 123 Fed. 396;
Columbia Graphophone Co. vs. Searchlight
Horn Co., 236 Fed. 135, 9;
Vineyard L. & S. Co. vs. Twin Falls Oakley
L. & W. Co., 245 Fed. 30, 33.

If it can be said that there is any conflict in the testimony (and there is actually very little conflict) then all such conflict has been resolved by the trial judge in favor of appellants and the decision of the trial judge in respect to the evidence is persuasive and presumptively correct.

Presidio Min. Co. vs. Overton, 270 Fed. 388;
Pac. Amer. Fish. vs. Hoff, 291 Fed. 306;
Conqueror Trust Co. vs. F. & D. Co. of Maryland, 63 Fed. (2d) 833, 7;
Woods-Faulkner & Co. vs. Michelson, 63 Fed. (2d) 569, 70;
Clements vs. Coppin, 61 Fed. (2d) 552, 7;
McCullogh vs. Penn. Mut. Life Ins. Co. of Phila., 62 Fed. (2d) 831;
U. S. Etc. vs. McGowan, 62 Fed. (2d) 955;
Collins, et al., vs. Finley, 65 Fed. (2d) 625.

For the reasons foregoing, appellants respectfully submit that the judgment should be reversed and a

judgment in favor of appellants for the relief prayed for should be ordered.

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Missoula, Montana,
S. P. WILSON,
Deer Lodge, Montana,
Attorneys for Appellants.

APPENDIX

Section numbers hereinafter set forth refer to Revised Codes of Montana 1921, unless otherwise specified.

7093. *What waters may be appropriated.* The right to the use of the unappropriated water of any river, stream, ravine, coulee, spring, lake, or other natural source of supply may be acquired by appropriation, and an appropriator may impound flood, seepage, and waste waters in a reservoir and thereby appropriate the same.

7094. *Appropriation must be for a useful purpose.* The appropriation must be for some useful or beneficial purpose, and when the appropriator or his successor in interest abandons and ceases to use the water for such purpose, the right ceases; but questions of abandonment shall be questions of fact, and shall be determined as other questions of fact.

7095. *Point of diversion may be changed.* The person entitled to the use of water may change the place of diversion, if others are not thereby injured, and may extend the ditch, flume, pipe, or aqueduct, by which the diversion is made, to any place other than where the first use was made, and may use the water for other purposes than that for which it was originally appropriated.

7105. *Rights settled in one action.* In any action hereafter commenced for the protection of rights acquired to water under the laws of this state, plaintiff may make any or all persons who have diverted water from the said stream or source, parties to such action, and the court may in one judgment settle the relative priorities and rights of all the parties to such action. When damages are claimed for the wrongful diversion of water in any such action, the same may be assessed and apportioned by the jury in their verdicts, and judgment thereon may be entered for or against one

or more of several plaintiffs, or for or against one or more of several defendants, and may determine the ultimate rights of the parties between themselves. In any action concerning joint water rights, or joint rights in water ditches, unless partition of the same kind is asked by parties to the action, the court shall hear and determine such controversy as if the same were several as well as joint.

7128. *Effect of decree upon subsequent appropriations.* Whenever there shall have been an adjudication of the rights between appropriators or claimants to any stream or any other water supply in this state, in any district court of the state, or the United States court, in an action prosecuted in good faith between such appropriators or claimants to determine their respective rights to the use of such waters, and which decree is based upon evidence introduced, and not upon stipulations or admissions of the parties, such adjudication and decree, or certified copies thereof shall, as against all persons appropriating or diverting any of the waters of the said stream or other water supply, after the date of such decree, in an action relating to such waters, be prima facie evidence of the facts therein found, determined, and decree, respecting the rights of parties to said action to the use of the waters of said stream or other water supply.

Sections 7136, 7140, and 7150 as amended by Chapter 125, Laws of the Nineteenth Session of the Legislative Assembly 1925.

“Section 7136. Appointment of Water Commissioners. Whenever the rights of persons to use the waters of any stream, ditch or extension of ditch, watercourse, spring, lake, reservoir, or other source of supply have been determined by a decree or decrees of a court of competent jurisdiction, it shall be the duty of the judge of the district court having jurisdiction of the subject mat-

ter, upon the application of the owners of at least ten per cent of the water rights affected by the decree or decrees, in the exercise of his discretion, to appoint one or more commissioners, who shall have authority to admeasure and distribute to the parties bound by the decree or decrees the waters to which they are entitled, according to their rights as fixed by such decree or decrees. At the time of the appointment of any water commissioner or water commissioners, his or their fees and compensation must be fixed in the order.”

“Section 7140. Power of Commissioners in Admeasuring Water Expenses. Every water commissioner appointed by the judge of the district court for that purpose shall have the authority to admeasure and distribute to the parties interested, under such decree or decrees, the water to which those who are parties to the decree or decrees, or privy thereto, are entitled according to their priority as established by the decree or decrees. The water commissioner, in case the parties fail or refuse to do so, may incur necessary expenses in the making of headgates or dams for the distribution of the waters, and such expense shall be assessed against and paid by the party or parties for whom such services in the repair of the ditch or ditches, and the making of any dams or headgates, were necessary. Provided, that in the discretion of the court, such costs or expenses may be assessed against the land upon which or for the benefit of which such expense had been incurred.”

“Section 7150. Complaint by Dissatisfied User—Procedure. Any person owning or using any of the waters of such stream or ditch or extension of ditch, who is dissatisfied with the method of distribution of the waters of such stream or ditch by such water commissioner or water commissioners, and who claims to be entitled to more water than he is receiving, or is entitled to a right

prior to that allowed him by such commissioner or water commissioners, may file his written complaint, duly verified, setting forth the facts of such claim. Thereupon the judge shall fix a time for the hearing of such petition, and shall direct that such notice be given to the parties interested in such hearing as the judge may deem necessary. At the time fixed for such hearing, the judge must hear and examine the complainant and such other parties as may appear to support or resist such claim, and also examine such water commissioner or water commissioners and witnesses as to the charges contained in said complaint. Upon the determination of the hearing, the judge shall make such findings and order as he may deem just and proper in the premises. If it shall appear to the judge that the water commissioner or water commissioners have not properly distributed the water according to the provisions of the decree, then the judge shall give the proper instructions for such distribution. The judge may remove such water commissioner or water commissioners and appoint some other person or persons in his or their stead, if he deems that the interests of the parties in the waters mentioned in such decree will be best subserved thereby, and if it shall appear to the judge that the said water commissioner or water commissioners have wilfully failed to perform their duties, they may be proceeded against for contempt of court, as provided in contempt cases. The judge shall make such order as to the payment of costs of such hearing as may appear to him to be just and proper."

9015. *Seizin within ten years*—*When necessary in actions for real property*—*Action for dower*. No action for the recovery of real property, or for the possession thereof, can be maintained, unless it appear that the plaintiff, his ancestor, predecessor, or grantor, was seized or possessed of the property in question within ten years

before the commencement of the action. No action for the recovery of dower can be maintained by a widow unless the action is commenced within ten years after the death of her husband.

9041. *Actions for relief not hereinbefore provided for.* An action for relief not hereinbefore provided for must be commenced within five years after the cause of action shall have accrued.

United States
Circuit Court of Appeals
For the Ninth Circuit.

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

ELMER D. BRYSON,
Respondent.
and

ELMER D. BRYSON,
Petitioner,
vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Transcript of the Record

Upon Petitions to Review an Order of the United States
Board of Tax Appeals.

FILED

AUG -9 1934

PAUL P. O'BRIEN,

No. 7519

United States
Circuit Court of Appeals
For the Ninth Circuit.

GUY T. HELVERING, as Commissioner of
Internal Revenue,
Petitioner,
vs.

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Transcript of the Record

Upon Petition to Review an Order of the
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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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Docket No. 22255

APPEARANCES.

For Taxpayer:

JOHN F. WATSON, Esq.,
HERBERT C. BRYSON, Esq.,

For Comm'r.:

ELDON McFARLAND, Esq.

DOCKET ENTRIES.

1926

Dec. 31—Petition received and filed. Taxpayer notified.

1927

Jan. 3—Copy of petition served on General Counsel.

Mar. 4—Answer filed by General Counsel.

“ 22—Motion for judgment filed by taxpayer.

Apr. 5—Copy of answer served on taxpayer. Assigned General Calendar.

May 7—Request for field hearing in Washington state to be heard with docket 22184 at the same time and place. Granted 5/7/27.

1930

Apr. 16—Hearing set in Spokane, Washington, week beginning June 2, 1930.

May 8—Application for subpoena duces tecum filed by taxpayer.

“ 9—Application for subpoena duces tecum filed by taxpayer.

“ 16—Demand for documents filed by taxpayer.

1930

- May 13—Order that a subpoena issue for Commissioner of Internal Revenue duces tecum and that the application for subpoena insofar as it relates to the Collector of Internal Revenue, Tacoma, Washington and all officers having control of original documents, etc. be denied, entered.
- “ 13—Subpoena issued.
- “ 20—Order that respondent have at hearing certain specified documents entered.
- “ 24—Application for subpoena of Elmer D. Bryson filed by General Counsel.
- “ 24—Subpoena issued (duces tecum)
E. D. Bryson.
- “ 24—Application for subpoena of L. L. Robison.
- “ 24—Subpoena issued L. L. Robison.
- Jun. 2—Hearing held before Eugene Black, Div. 15 on merits. Consolidated with docket 22184. Briefs due in 90 days. Amendment to Answer allowed.
- Jul. 8—Transcript of hearing of June 2, 1930 filed.
- Aug. 19—Brief filed by taxpayer.
- “ 22—Motion for extension to 10/15/30 to file brief filed by General Counsel. See 22184.
- “ 25—Motion granted. [1*]
- Oct. 14—Motion for extension to 12/14/30 to file brief filed by General Counsel. 10/16/30 granted.
- Dec. 13—Brief filed by General Counsel.

*Page numbering appearing at the foot of page of original certified Transcript of Record.

1931

Feb. 26—Findings of fact and opinion rendered, Mr. Black, Div. 15. Decision will be entered under Rule 50.

Mar. 14—Petition for review by entire Board filed by taxpayer.

“ 14—Application for permission to make trial amendment filed by taxpayer.

“ 14—Application to reopen the case for additional evidence filed by taxpayer.

“ 14—Objection and exceptions filed by taxpayer.

“ 28—Memorandum opinion and order, Mr. Black, restored to calendar of 4/29/31 entered.

“ 28—Order denying motion for Board review entered.

Apr. 27—Brief filed by taxpayer.

“ 29—Stipulation as to return for Bryson—Robison Corporation for the years 1917 and 1918 filed.

“ 29—Hearing had before Mr. Black on motion for further hearing. Stipulation filed.

“ 30—Order allowing briefs 30 days from Apr. 29, 1931 to file briefs entered.

1932

Jul. 20—Memorandum opinion rendered Mr. Black, Div. 15. Decision will be entered that petitioner is not liable for any deficiency of Bryson Robison Corporation for years 1917 and 1918 but is liable for the year 1919 which will be redetermined in accordance with former opinion.

1932

Jul. 30—Motion to review findings promulgated July 20, 1932 filed by taxpayer.

“ 30—Objections and exceptions filed by taxpayer.

Aug. 4—Order denying motion for review of Memorandum Opinion entered.

“ 22—Motion for reconsideration and review by Board with brief in support thereof filed by General Counsel.

Sep. 22—Order denying motion to reconsider entered.

Oct. 31—Notice of settlement filed by General Counsel.

Nov. 2—Hearing set for Nov. 30, 1932 on settlement.

“ 22—Motion and affidavit for 30 days extension filed by taxpayer.

“ 25—Order of continuance to Jan. 4, 1932 on settlement entered.

Dec. 24—Objections to notice of settlement filed by taxpayer.

1933

Jan. 4—Hearing had before Mr. Black, Div. 15 on settlement under Rule 50.

“ 26—Decision entered, Mr. Black, Div. 15.

Apr. 19—Petition for review by U. S. Circuit Court of Appeals (9) with assignments of error filed by General Counsel.

May 4—Petition for review by U. S. Circuit Court of Appeals (9) with assignments of error filed by taxpayer.

“ 4—Proof of service filed by General Counsel.

1933

May 4—Proof of service filed by taxpayer.

“ 12—Affidavit of service filed by taxpayer.

“ 13—Motion to vacate final order filed by taxpayer. [2]

May 22—Order denying motion to vacate entered.

Jun. 13—Motion for extension to 7/15/33 to complete record filed by General Counsel.

“ 13—Order enlarging time to July 15, 1933 for preparation and delivery of record entered.

Jun. 20—Statement of evidence lodged. (General Counsel)

“ 28—Praecipe filed by taxpayer.

“ 28—Cross appellant and respondent's additional statement of evidence lodged.

“ 28—Notice of lodgment of statement and of hearing July 20, 1933 filed.

“ 30—Praecipe with proof of service thereon filed by General Counsel.

“ 30—Notice of lodgment of statement and of hearing July 20, 1933 to approve statement filed.

“ 29—Notice changing hearing date from July 20, 1933 to July 19, 1933.

Jul. 10—Petitioner's objection to cross appellant and respondent's additional statement of evidence filed.

“ 10—Motion for extension to Aug. 15, 1933 to complete record filed by General Counsel.

“ 10—Objection to cross appellant and respondent's praecipe for record filed by General Counsel.

1933

- Jul. 10—Order enlarging time to August 15, 1933 for preparation of evidence and delivery of record entered.
- “ 19—Hearing had before Mr. Black, Div. 15 on approval of statement of evidence. Agreed statement to be filed.
- “ 25—Order denying cross appellant and respondent on review’s request for additional statement of evidence entered.
- “ 25—Order determining praecipe for record—further ordered that Board’s order of May 22, 1933 be included as part of record entered.
- “ 25—Statement of evidence approved and ordered filed.
- Aug. 12—Motion for extension to 10/1/33 to complete record filed by General Counsel.
- “ 12—Order enlarging time to Oct. 2, 1933 for preparation of evidence and delivery of record entered.
- Oct. 2—Motion for extension to Nov. 1, 1933 to complete record filed by General Counsel.
- “ 2—Order enlarging time to Nov. 1, 1933 for preparation of evidence and delivery of record entered.
- “ 30—Motion for extension to Jan. 1, 1934 to prepare and complete record filed by General Counsel.
- “ 30—Order enlarging time to Jan. 1, 1934 for preparation of evidence and delivery of record entered.

1933

Dec. 29—Motion for extension to 3/1/34 to complete record filed by General Counsel.

Dec. 29—Order enlarging time to 3/1/34 for preparation of evidence and delivery of record entered.

1934

Feb. 17—Motion for extension to May 1, 1934 to complete and transmit record filed by General Counsel.

“ 17—Order enlarging time to May 1, 1934 for preparation of evidence and delivery of record entered.

May 1—Order enlarging time to June 15, 1934 for transmission and delivery of record entered. [3 & 4]

United States Board of Tax Appeals

Docket No. 22255

ELMER D. BRYSON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION.

The above named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency IT:E:RR-280-60D HTL dated November 3, 1926, and as a basis of his proceeding alleges as follows:

1. The petitioner is Mr. Elmer D. Bryson, an individual, with principal residence at 605 Boyer Avenue, Walla Walla, Washington.

2. The notice of deficiency (a copy of which is attached and marked Exhibit A) was mailed to the petitioner on the third day of November, 1926.

3. The taxes in controversy are income and profits taxes levied against the Bryson-Robison Corporation, Walla Walla, Washington, in the total sum of \$11,578.85 assessed against such company for the years 1917, 1918 and 1919. The proposed assessment against which this petition for a re-determination is made is in the sum of \$5,789.43, being one half of the assessment, and such proposed assessment is based upon the liability of the petitioner under Section 280 of the Revenue Act of 1926, as a transferee of property of the Bryson-Robison Corporation, which ceased to do business on about June 4, 1919.

4. The determination of tax set forth in the said notice of deficiency is based upon the following errors:

First: That all of said proposed assessment against the petitioner is barred by operation of the Statute of Limitations.

Second: That the Commissioner of Internal Revenue in arriving at the amount of the invested capital of the Bryson-Robison Corporation erroneously reduced the said invested capital by the sum of \$45,000.00.

Third: That the Commissioner in arriving at the net income of the Bryson-Robison Corporation in

error disallowed the salaries of the corporation officers for the years 1917 and 1919. That said lawful and proper deduction for salaries during 1917 was the sum of \$10,000.00, (the same as allowed in 1918), and for 1919 was at the rate of \$10,000.00 per year up until June 4, 1919 when the company ceased to operate as a going concern. Disallowing said salaries was in error. [5]

Fourth: That the several income tax returns for the years 1917, 1918 and 1919 as made and filed by Bryson-Robison Corporation were true and correct as to amounts and items of all receipts, disbursements and legal deductions allowable for each of said years, and the Commissioner erred in disregarding and setting aside said income tax returns and the tax as therein computed and accepting in lieu thereof some book "set up" unauthorized by said corporation, without the knowledge of said corporation or any of its duly authorized officers the correctness of which said set up your petitioner believes to be unreliable.

Fifth: The Commissioner erred in determining petitioner to be a transferee of one half the assets of the corporation of Bryson-Robison Corporation on dissolution thereof as petitioner purchased of and from Lester L. Robison and said corporation certain assets, being all of the assets, of said corporation as an independent, outright purchase.

5. The facts upon which the petitioner relies as a basis of this proceeding are as follows:

(a) That no assessment of said taxes for said years 1917, 1918 and 1919 or any of them has been made against said Bryson-Robison Corporation, or the petitioner within the time limited by the Revenue Laws.

(b) That petitioner has never signed a waiver of the statute of limitations as an individual, and that no authorized or valid waiver has ever been submitted by said Bryson-Robison Corporation.

(c) That the Bryson-Robison Corporation was organized under the laws of the State of Washington in 1916 and commenced business on October 16, 1916. That as stated in the Revenue Agents Report made under date of Oct. 22, 1923, this corporation purchased lands at a cost of \$45,000.00. For good and sufficient reasons not material to this case the corporation on Mar. 1, 1917, deeded this land to Lester L. Robison and Elmer D. Bryson, to be held by them in trust for the corporation; two days later, on March 3d, 1917, Lester L. Robison and Elmer D. Bryson deeded said land back to the corporation. The deeds from Lester L. Robison and Elmer D. Bryson were not recorded but were placed in escrow in the law office of Goss & Crowe, Walla Walla, Washington. No money changed hands on either transaction. At all times before and after the said transaction the land was treated and considered as belonging to the said corporation, the company paying for the improvements thereon and paying the taxes thereon; having no lease and paying no rent for the use of the land. That the company at all

times had actually invested in said lands as shown by the Revenue Agents report the sum of \$45,000.00. That in the event the deed did convey the property from the assets of the company, then accounts receivable of the value of \$45,000.00 replaced the land in the assets of the company and the invested capital would not be reduced by the transaction. The land was not given away and there was no dividend declared of the land. Therefore, if it is held that the company lost title to the land, it must be held that they gained title to perfectly good accounts receivable in the sum of \$45,000.00 from Lester L. Robison and Elmer D. Bryson. The invested capital should not therefore be reduced in any amount by the transaction.

(d) That shortly after the corporation commenced business in 1916 it was agreed that the two officers of the company, Lester L. Robison and [6] Elmer D. Bryson, should receive annually as salaries the sum of \$5,000 each. These said officers managed the corporation entirely and the salaries were reasonable and in accord with the services rendered. Both officers were experienced farmers and sheep men and as shown by the profits were competent to draw \$5000 salaries. No set of books was kept by the company; the cancelled checks and balance sheets being the source of information in the audit. At the end of 1917 the company had not made sales so that the salaries could be paid and since there were no books, no credits to the officer managers could be made for salaries. During 1918, following sales of

products, distribution of money was made to the said officers. Of the amounts distributed the Revenue Agent and the Commissioner has allowed to be treated as salaries the sum of \$5000 to each of the named officers. But the \$5000 due each of them as salaries for 1917 has been treated as dividends distributed in 1918. This action is in error and most unjust to the taxpayer. When the company sold out on June 4, 1919 there was due the named officers salaries at the rate of \$5,000 per year up to that date and a deduction for same should be allowed in arriving at the net income of the company. Both officers actually received the money for the salaries for all years, but because of their ignorance of the income tax law and of methods of accounting the money was paid to them in a manner which makes it complicated to designate as a salary payment. The salary deduction was authorized by the directors who were the officers and stockholders, the salaries were actually paid and are an allowable deduction for income and excess profits tax purposes.

(e) The Bryson-Robison Corporation was a sheep farming company, whose officers were practical and experienced stockmen without knowledge or experience in accounting or of income tax laws, rules and regulations. The only business records kept by the corporation were adequate for their purposes of the business, but were only their bank records of deposit for gross sales and their bank checks record of all disbursements for corporate purposes. The corporation at no time, nor did any duly authorized

officer of the corporation, either compile or "set up", nor authorize compilation and setting up of a book record in accounting form of its transactions as a corporation, and petitioner has no accounting knowledge sufficient to form a belief as to the technical accounting accuracy of the "set up" apparently used by the auditor for the Commissioner. Petitioner alleges that the original income tax returns, with farm schedules, were correct in amount and should have been accepted.

(f) The petitioner purchased assets of the corporation from Lester L. Robison and the corporation, not as a stockholder, but as an independent purchaser paying his own money therefor.

WHEREFORE, the petitioner prays that this Board may hear the proceeding and find: that petitioner is not liable for any proposed tax assessment because of same being barred by the running of the Statute of Limitations as provided in the Revenue Laws; that the Commissioner was in error in reducing the invested capital of the Bryson-Robison Corporation in the amount of \$45,000 during the year 1917; that the Commissioner was in error in disallowing to the Bryson-Robison Corporation a salary deduction in 1917 in the amount of \$10,000; and that the Commission was in error in disallowing to the corporation a salary reduction [7] in 1919 in the amount of at least \$4,200.

HERBERT C. BRYSON,
Counsel for Petitioner
312-13 Drumheller Bldg.,
Walla Walla, Washington.

State of Washington,
County of Walla Walla—ss.

Elmer D. Bryson, being duly sworn, says that he is the petitioner above named, that he has read the foregoing petition and is familiar with the statements contained therein, and that the facts stated are true.

ELMER D. BRYSON

Subscribed and sworn to before me this 28th day of December, 1926.

[Seal]

HERBERT C. BRYSON,
Notary Public for Washington, residing
at Walla Walla. [8]

TREASURY DEPARTMENT

Office of

Commissioner of Internal Revenue

Washington,

November 3, 1926.

IT:E:RR-280-60D

HTL

Mr. Elmer D. Bryson,
605 Boyer Avenue,
Walla Walla, Washington.

Sir:

As provided in Section 280 of the Revenue Act of 1926, there is proposed for assessment against you the amount of \$5,789.43, constituting your liability as a transferee of the property of the Bryson-Robi-

son Corporation, Walla Walla, Washington, for unpaid income and profits taxes in the amount of \$11,578.85 assessed against such company for the years 1917, 1918 and 1919, as per the attached statement, plus any accrued penalty and interest.

In accordance with the provisions of Section 274 of the Revenue Act of 1926, you are allowed 60 days from the date of mailing of this letter within which to file a petition for the redetermination of this deficiency. Any such petition must be addressed to the United States Board of Tax Appeals, Earle Building, Washington, D. C., and *must mailed* in time to reach the Board within the 60-day period, not counting Sunday as the sixtieth day.

Where a taxpayer has been given an opportunity to file a petition with the United States Board of Tax Appeals and has not done so within the 60 days prescribed and an assessment has been made, or where a taxpayer has filed a petition and an assessment in accordance with the final decision on such petition has been made, the unpaid amount of the assessment must be paid upon notice and demand from the Collector of Internal Revenue. No claim for abatement can be entertained.

If you acquiesce in this determination and do not desire to file a petition with the United States Board of Tax Appeals, you are requested to execute a waiver of your right to file a petition with the United States Board of Tax Appeals on the inclosed Form A, and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the atten-

tion of IT:C:P-7. In the event that you acquiesce in a part of the determination, the waiver should be executed with respect to the items to which you agree.

Respectfully,
D. H. BLAIR,
Commissioner.

By C. R. NASH,
Assistant to the Commissioner.

Inclosures:

Statement
Form A [9]

Mr. Elmer D. Bryson, Transferee

STATEMENT

IT:E:RE-280-60D

HTL

In re: Bryson-Robison Corporation,
Walla Walla, Washington.

1917

Additional tax assessed on March 1924 List, Page O, Line 4	\$5,896.86
Abatement allowed, September 18, 1925, Schedule 15439	3,033.44
	<hr/>
Deficiency in tax	\$2,863.42

1918

Net income as by a supplemental examination of
your books of account and records \$20,636.45

As the tax computed under Section 301 of the Revenue Act of 1918 is in excess of the tax computed under Section 302 of that Act, it is computed under the latter section, as follows:

Net income, as above \$20,636.45

Less:

Income not in excess of the limitation
of the 30% tax 20,000.00

Balance taxable at 80% \$ 636.45

Net income not in excess of the
limitation of the 30% tax \$20,000.00

Less:

Exemption 3,000.00

Balance taxable at 30% \$17,000.00

Tax at 30% 5,100.00

Tax at 80% 509.16

Total profits tax \$5,609.16

Net income \$20,636.45

Less:

Profits tax \$5,609.16

Exemption 2,000.00 7,609.16

Balance taxable at 12% \$13,027.29

Tax at 12% 1,563.27

Total tax assessable \$7,172.43

[10]

Brought forward \$7,172.43

Original tax assessed on Account No. 438626,
dated June, 1919 1,430.54

Additional tax due \$5,741.89

You are informed that your contention that the value of land, title to which is vested in the indi-

vidual stockholders, should be included in your invested capital has not been conceded by this office. There is no provision in the income tax laws which authorizes a taxpayer to include in invested capital property which it does not own.

Your contention that, as a matter of equity, you should be allowed as a deduction for officers' salaries \$5,000.00 for 1917 has not been allowed for the reason that the amount was not paid or accrued during 1917, and, therefore, is specifically disallowable under T. B. M. 86.

1919

Net income, Revenue Agent's report	\$13,271.57
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Inasmuch as the tax when computed under Section 301 is in excess of that computed under the provisions of Section 302, the tax is computed under the latter section as follows:

Net income	\$13,271.57
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Less:

Exemption	3,000.00
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Balance taxable at 20%	\$ 9,271.57
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Total profits tax, Section 302	\$2,054.31
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Net income	\$13,271.57
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Less:

Profits tax	\$2,054.31
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Exemption	2,000.00	4,054.31
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Taxable at 10%	\$ 9,217.26	921.73
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Total tax assessable	\$2,976.04
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Tax previously assessed:

Account No. 402204	2.50
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Additional tax due	\$2,973.54
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[Endorsed]: United States Board of Tax Appeals.
Filed Dec. 31, 1926. [11]

[Title of Court and Cause.]

ANSWER.

The Commissioner of Internal Revenue by his attorney, A. W. Gregg, General Counsel, Bureau of Internal Revenue, for answer to the petition of the above named taxpayer admits and denies as follows:

(1) The first three paragraphs of the petition are admitted.

(2) It is denied that the Bryson-Robison Corporation may include as a part of its invested capital for the years 1917, 1918 and 1919, an item of \$45,000.00 alleged to represent the value of real estate. It is denied that the said corporation owned the legal title to or the equitable title in said real estate, so as to permit the same to be treated as a part of its invested capital.

(3) It is denied that the Bryson-Robison Corporation authorized, paid or accrued during the years 1917 to 1919 inclusive the amount of \$5000.00 each as compensation to its two officers; and it is denied that said amounts may be claimed or allowed as deductions in computing the income of said corporation for said years.

(4) At the time the assessments were made against said corporation for additional taxes for the year 1917 to 1919 inclusive, it is denied that such assessments were inhibited or barred by the Statute of Limitations; and it is denied that the assessments that have been made against said corporation are not in all things proper. [12]

(5) It is denied that the petitioner is not a transferee of the assets of the said Bryson-Robison Corporation, within the meaning of Section 260 of the Revenue Act of 1926, and liable for the deficiency in tax due and owing by said corporation; and it is denied that due and proper notice has not been given to him for such liability.

(6) Denies generally and specifically each and every allegation contained in the taxpayer's petition not hereinbefore admitted, qualified or denied.

WHEREFORE, it is prayed that the taxpayer's petition be dismissed and the appeal denied.

A. W. GREGG,
General Counsel,
Bureau of Internal Revenue.

Of Counsel:

ROBERT A. LITTLETON,
Special Attorney,
Bureau of Internal Revenue.

[Endorsed]: United States Board of Tax Appeals.
Filed Mar. 4, 1927. [13]

[Title of Court and Cause.]

AMENDMENT TO ANSWER.

Comes now the Respondent above named and having first had and obtained leave so to do, amends his answer in the above-entitled cause as follows:

1. By striking paragraph 2 of said answer and substituting therefor the following, to-wit:

Answering the allegations contained in subdivision "second" of paragraph 4 of the petition herein, admits that the Commissioner of Internal Revenue failed and refused to allow as invested capital of Bryson-Robison Corporation, in computing said corporation's income and profits taxes for the years 1917, 1918 and 1919, *respectfully*, the sum of \$45,000.00; denies that such failure or refusal to allow said sum as invested capital was erroneous.

2. By adding the following paragraph, to-wit:

4(a) Answering the allegations contained in subdivision (c) of paragraph 5 of the petition herein, admits that Bryson-Robison Corporation transferred certain real property on or about March 1, 1917, by deed to Lester L. Robison and Elmer D. Bryson to be held by said grantees in trust for said corporation; admits that on or about March 1, 1917, Lester L. Robison and Elmer D. Bryson deeded said land back to said corporation; denies, generally and specifically, the remaining allegations in subdivision (c) of paragraph 5 of said petition. [14]

As a further, separate and distinct defense, Respondent alleges:

1. Refers to all the allegations contained in the petition herein except the allegations denied by Respondent's answer as amended and by such reference incorporates said allegations herein with the same force and effect as if set forth here at length.

2. Alleges that the Commissioner of Internal Revenue duly assessed against Bryson-Robison Corporation the additional taxes set forth on pages

two and three of the sixty-day letter, a copy of which is attached to the petition herein and marked Exhibit "A", as follows:

Deficiency in tax, 1917, after deducting abatement allowed,	\$ 2,863.42
Deficiency for 1918,	5,741.89
Deficiency for 1919,	2,973.54
<hr/>	
Total,	\$11,589.85

3. That said taxes have not been paid nor any part thereof.

4. Basing his allegations upon information and belief, Respondent alleges that on or about June 4, 1919, said corporation conveyed and transferred to petitioner herein and to one Lester L. Robison without consideration, all of its assets.

5. That the value of the assets transferred from said corporation to petitioner as aforesaid was in excess of \$11,588.85.

6. That said corporation ever since said transfer has been and now is without any assets whatever.

7. That said corporation has forfeited its charter and is dissolved.

8. That by reason of the premises the petitioner is liable for the entire sum of said deficiency of income and profits taxes for the years 1917 to 1919, inclusive, in the total amount of \$11,588.85. [15]

9. That the Commissioner of Internal Revenue erred in proposing, in the sixty-day letter of November 3, 1926, a copy of which is attached to the petition and marked Exhibit "A", assessment of

only one-half of said deficiencies instead of the entire amount thereof, against petitioner herein.

WHEREFORE, Respondent prays for a determination that the entire deficiencies of \$2,863.42 for the year 1917, \$5,741.89 for the year 1918 and \$2,973.54 for the year 1919, should be assessed against petitioner herein as transferee of the assets of Bryson-Robison Corporation.

.....
General Counsel,
Bureau of Internal Revenue.

Of Counsel:

ELDEN McFARLAND,
ARTHUR CLARK,
Special Attorneys,
Bureau of Internal Revenue.

[Endorsed]: United States Board of Tax Appeals.
Filed at hearing Jun. 2, 1930. [16]

[Title of Court and Cause.]

Dockets Nos. 22184 and 22255.
Promulgated February 26, 1931.

FINDINGS OF FACT AND OPINION.

1. Transferee—Held petitioner Lester L. Robison not liable as transferee. Petitioner Elmer D. Bryson liable as transferee.

2. Increase of Deficiency—Section 308 (e) of the Act of 1926 gives the Board jurisdiction to increase the deficiency over that determined

by the Commissioner, if asserted by the Commissioner before or at the hearing, and the action of the Board in permitting respondent to amend his answer to that effect is not error.

3. Limitation—The burden of proof to establish the plea of limitation is on petitioners and where it is not shown when the return was filed the plea of limitation must fail, for lack of evidence to support it.

4. Tax Settlement—Petitioner's action in approval of a Revenue Agent's report does not establish a closing agreement under either Section 3229, Revised Statutes, or Section 606, Revenue Act of 1928.

5. Claims for invested capital and salaries allowed in part.

John F. Watson, Esq., and Herbert C. Bryson, Esq.,
for the petitioners.

J. E. McFarland, Esq., for the respondent.

These two cases were consolidated for hearing and decision. They involve deficiencies in income and profits taxes determined against the Bryson-Robison Corporation of \$2,863.42 for 1917; \$5,741.89 for 1918 and \$2,973.54 for 1919, and now sought to be collected from the petitioners as transferees of the assets of the taxpayer. The total amount of the defi- [17] ciencies was \$11,578.85. In his deficiency letter the respondent only proposed one-half thereof, viz., \$5,789.42 against each transferee, but at the hearing, by permission of the Board, filed amended answers increasing the claim against each

petitioner to the full amount. Errors complained of by the petitioners will be fully stated in the Opinion.

FINDINGS OF FACT.

The petitioner, Lester L. Robison, is an individual and resides at R. F. D. #4, Walla Walla, Washington, and the petitioner, Elmer D. Bryson, is an individual and resides at 605 Boyer Avenue, Walla Walla, Washington. In 1916, the taxpayer Bryson-Robison Corporation was organized under the laws of the State of Washington for the purpose of engaging in farming, raising sheep and the operation of a sheep ranch. Its capital stock was \$100,000.00 divided equally between the petitioners, except that the wife of each held one share each for organization and qualification purposes. The corporation engaged in business until June 4, 1919, when the petitioner Elmer D. Bryson purchased the stock and interest of the petitioner Lester L. Robison in the corporation for the sum of \$70,000.00, took possession of its entire assets and operated the business thereafter as an individual. Prior to the sale by Robison of all his shares of stock in the corporation to Bryson, to-wit, on April 22, 1919, a petition to dissolve the corporation was filed in the Superior Court for Walla Walla County, but no final judgment was ever entered. However, it became dissolved by operation of the laws of the State of Washington, as will be seen by the certificate of the Secretary of State of the State of Washington, dated May 14, 1930, and reading as follows:—

I, J. Grant Hinkle, Secretary of State of the State of Washington and custodian of the Seal of said State, do hereby certify that I have carefully examined the records of this [18] office and find that the "Bryson-Robison Corporation", a domestic corporation of Walla Walla, Washington, filed a copy of its articles of incorporation in this office on the 13th day of October, 1916.

I further certify that the above mentioned corporation was stricken from the records of this office July 1, 1921, and was further "Stricken from Records and dissolved" July 1, 1924 under the provisions of Chapter 144, Laws of Washington of 1923, for failure to pay the annual license fees and accruing penalties, the last license fee paid being for the fiscal year ending June 30, 1919.

And I further certify that the above mentioned corporation has had no legal corporate existence since stricken July 1, 1921, pursuant to Chapter 140, laws of 1907.

Upon its organization the corporation purchased certain lands at a cost of \$40,000.00 for its business purposes. Other smaller tracts were afterwards purchased, but the cost was not shown.

No formal corporate meetings were held and no regular set of books or accounts were kept. The principal records of the corporation were canceled checks and sheets of paper showing receipts and disbursements of the corporation. Robison was

President and Bryson was Secretary and Treasurer. In verbal agreement it was understood that each should receive a salary of \$5,000 per year. This was paid for the year 1918, but none was paid in 1917 or in 1919. Petitioners devoted most of their time to the business performing various duties connected with the business during the taxable year up to June 4, 1919, when the corporation ceased to do business. A reasonable allowance for salary for 1917 is \$2,500 for each petitioner and for 1919 until June 4 an allowance of \$2,500 in full for both petitioners, or \$1,250 each, is reasonable.

There is no evidence in the record as to the date of the filing of the tax returns of the corporation for the taxable years 1917 and 1918. That for 1919 was filed March 15, 1920, and was signed by petitioner [19] "Elmer D. Bryson, sole remaining officer". On February 12, 1923, a one year waiver for the Bryson-Robison Corporation for 1917 was executed and reads as follows:—

INCOME AND PROFITS TAX WAIVER.

Feb. 12, 1923.

In pursuance of the provisions of subdivision (d) of Section 250 of the Revenue Act of 1921, Elmer D. Bryson, of Walla Walla, Wash., and the Commissioner of Internal Revenue, hereby consent to a determination, assessment, and collection of the amount of income, excess-profits, or war-profits taxes due under any return made by or on behalf of the said Bryson-Robison Cor-

poration for the year 1917 under the Revenue Act of 1921, or under prior income, excess-profits, or war-profits tax Acts, or under Section 38 of the Act entitled "An Act to provide revenue, equalize duties, and encourage the industries of the United States, and for other purposes", approved August 5, 1909, irrespective of any period of limitations.

This waiver will be effective only one year from date of signing

(Sgnd) Elmer D. Bryson,

Taxpayer,

as former Secretary—Bryson-Robison Corp.

(Sgnd) D. H. Blair, c.

Commissioner.

On January 2, 1924, an unlimited waiver for 1917 and 1918 for the corporation was executed and reads as follows:

INCOME AND PROFITS TAX WAIVER.

In pursuance of the provisions of subdivision (d) of Section 250 of the Revenue Act of 1921, Bryson-Robinson Corp., of Walla Walla, Washington and the Commissioner of Internal Revenue, hereby consent to a determination, assessment and collection of the amount of income, excess-profits, or war-profits taxes due under any return made by or on behalf of the said Corporation for the years 1917 and 1918 under the Revenue Act of 1921, or under prior income, excess-profits, or war-profits tax Acts, or under Section 38 of the Act entitled "An Act

to provide revenue, equalize duties, and encourage the industries of the United States, and for other purposes'', approved August 5, 1909, irrespective of any period of limitations.

(Sgnd) Elmer D. Bryson,
Former Secretary of the Bryson-Robison Corp.

Taxpayer,

(Sgnd) D. H. Blair, c.

Commissioner.

The deficiencies were assessed against the taxpayer corporation as [20] follows:—for 1917 on March 21, 1924; for 1918 on September 1, 1925, and for 1919 on March 14, 1925. These assessed taxes remain unpaid. The sixty day letters to the petitioners as transferees were mailed November 3, 1926. The net value of the assets transferred to Bryson exceeded the amount of the deficiencies.

OPINION.

BLACK:—Each of the petitioners based his appeal on the following assignments of error:

That the Commissioner of Internal Revenue in arriving at the amount of the invested capital of the Bryson-Robison Corporation erroneously reduced the said invested capital by the sum of \$45,000.00.

That the Commissioner in arriving at the net income of the Bryson-Robison Corporation in error disallowed the salaries of the corporation officers for the years 1917 and 1919. That said lawful and prior deduction for salaries during

1917 was the sum of \$10,000, (the same as allowed in 1918), and for 1919 was at the rate of \$10,000 per year up until June 4, 1919 when the company ceased to operate as a going concern. Disallowing said salaries was in error.

The Commissioner erred in determining petitioner to be a transferee of one-half the assets of the corporation of Bryson-Robison Corporation on dissolution thereof.

That all of said proposed assessment against the petitioner is barred by operation of the Statute of Limitations.

In addition to the foregoing assignments of error, each of the petitioners complain of the action of the Board in allowing respondent at the hearing to amend his answer and assert a liability against each petitioner for all of the deficiency determined against the transferor corporation, instead of the assertion of a liability for one-half of the deficiency against each petitioner contained in the sixty day letter mailed to each of said petitioners November 3, 1926. We think the allowance of the amendment was proper. Section 308 (e) of the Revenue Act of 1926. *Louis M. Weiller*, 18 B. T. A. 1121.

Petitioners' assignment of error that respondent erred in failing to include as invested capital of the taxpayer for the taxable years certain [21] real estate belonging to it, which it had purchased with funds belonging to the corporation, is sustained to the extent of the costs of such lands, proved at the hearing. Respondent, by amended answer filed at

the hearing, confessed error in failing to allow the costs of such lands as a part of the corporation's invested capital, but contested the amount of costs claimed. Petitioners claim the value of the land at \$45,000 or over, and ask that the invested capital of the corporation be increased by that amount. Petitioners proved that \$40,000 was paid for 10,360 acres of land used in the corporation's business. It was also proved that the corporation purchased other small tracts of land, but no evidence was offered as to the cost thereof. We cannot allow as a part of the corporation's invested capital, assets, the cost of which is not proved. In view of the admissions by respondent in his amended answer, invested capital should be increased by \$40,000 over that which respondent allowed in his deficiency letters. Any increment in value over cost may not be included in invested capital. *La Belle Iron Works*, 256 U. S. 377.

Relative to the claim for salaries for 1917 and from January 1, 1919, to June 4, 1919, we think the evidence is sufficient to show that the amounts set out in our Findings of Fact would represent a reasonable allowance to the corporation for salaries incurred for personal services actually rendered to it during the period of time therein mentioned by Robison, President, and Bryson, Secretary-Treasurer. The respondent will make this allowance in recomputing the deficiency.

As to whether petitioners are liable as transferees, we think the facts show that Robison is not liable as a transferee, but that Bryson is so liable, under the

applicable statutes and the decisions of this Board. The attorney who represented the corporation in its various legal matters testified that Robison sold his stock to Bryson and that such stock was actually transferred [22] to Bryson. This statement of the transaction seems to be well supported by the other evidence in the proceeding. There is nothing to show that prior to his sale of stock to Bryson, Robison received one-half of the assets of the corporation in liquidation and then sold these assets to Bryson. On the contrary, the facts show that Robison sold his stock and interest in the corporation to Bryson for \$70,000; whereupon Bryson took over all the assets of the corporation and assumed all of its liabilities and from that time on, operated the business as an individual and not as a corporation. We hold that Robison is not a transferee of the corporation. The mere sale of stock by a stockholder in a corporation does not make him a transferee of the assets of the corporation. But the action of Bryson taking over all the assets of the corporation and assuming all of its liabilities, makes him a transferee of the assets of such corporation and liable as such. *J. W. Oglesby*, 16 B. T. A. 1191; *Frank Shloudeman*, 21 B. T. A. 605; *John Gerasom, et al*, 21 B. T. A. 1234.

Limitation is pleaded as to the deficiencies determined against the transferor corporation for each of the taxable years and the validity of the waivers is vigorously attacked in briefs of counsel. The burden of proof is upon the petitioners to establish

the plea of the statute of limitations and this requires first proof of date of the filing of the statutory returns and second, the expiration of the statutory period. There is no evidence of the date of the filing of the statutory returns of the corporation for either 1917 or 1918 and for that reason the plea of limitation must fail for those years. *Edward M. Lawrence*, 3 B. T. A. 40; *E. J. Lorie*, 21 B. T. A. 612. Petitioners in their briefs refer to the assessment lists introduced in evidence by the respondent, showing that the deficiencies determined against the transferor corporation for each of the taxable years were duly assessed, but these assessment lists do not in any way show when the corporations' tax returns for 1917 [23] and 1918 were filed. We are without any evidence on this point.

Under these circumstances it is immaterial whether the two waivers are valid or not. Even if we should hold them to be invalid, we have no evidence before us which would support petitioner's plea of limitation.

Relative to the taxable year 1919, that return was introduced in evidence and shows that it was filed March 15, 1920, and the assessment against the taxpayer corporation made March 14, 1925, which was in time.

Section 280 (b) (2), Revenue Act of 1926, provides: "If the period of limitation for assessment against the taxpayer expired before the enactment of this Act but assessment against the taxpayer was made within such period,—then six years after the

making of such assessment against the taxpayer, but in no case later than one year after the enactment of this Act." See also Section 278 (d) Revenue Act of 1926.

The Act of 1926 was effective February 26, 1926, and one year thereafter was February 26, 1927. The deficiency letters in this case, asserting liabilities against the respective petitioners, were mailed November 3, 1926, and were in time.

Counsel for petitioner Bryson urges in his brief an alleged settlement in behalf of his client. Failure to recognize such a settlement was not alleged as an error in the petition and the rule is that an issue argued in brief of counsel, but not raised in the pleadings will be disregarded. There is no evidence in the record of any settlement either under Section 3229, Revised Statutes, or Section 606, Revenue Act of 1928. The document urged by petitioner Bryson as supporting his contention that a settlement was made, is simply a report of a revenue agent recommending a refund of [24] \$7.45 for 1920 and no change for 1919. This is no closing agreement as contemplated under the applicable Revenue Acts. *Oilbelt Motor Co.*, 16 B. T. A. 831.

As to petitioner Lester L. Robison, decision will be entered that there is no liability as transferee.

As to petitioner Elmer D. Bryson, decision will be entered under Rule 50.

[Seal]

[Endorsed]: United States Board of Tax Appeals. A true copy: Teste. B. D. Gamble, Clerk. [25]

[Title of Court and Cause.]

Docket Nos. 22255 and 22184.

John F. Watson, Esq., and Herbert C. Bryson, Esq.,
for the petitioners.

J. E. McFarland, Esq., for the respondent.

MEMORANDUM OPINION AND ORDER.

BLACK: Findings of fact and opinion in this proceeding were promulgated February 26, 1931, and pursuant thereto decision was entered February 26, 1931, that there was no liability of petitioner, Lester L. Robison, as transferee in respect of the tax of the Bryson-Robison Corporation for the years 1917, 1918 and 1919. Final decision under Rule 50 has not yet been entered as to petitioner Elmer D. Bryson.

On March 14, 1931, petitioner, Elmer D. Bryson, filed his motion to reopen this proceeding for additional evidence. As reasons why the proceeding should be reopened for additional evidence, petitioner urges three grounds:

(1) Statute of limitations as to 1917 and 1918. Petitioner claims that the Board erred in its findings of fact in stating that the income tax returns of the Bryson-Robison Corporation for 1917 and 1918 were not introduced in evidence. Petitioner Bryson claims that these returns [26] were in fact introduced in evidence at the hearing held at Spokane, Washington, June 2, 1930, and were received as exhibits in the case.

An examination of the record shows that petitioner Bryson is in error in this contention. An

examination of the record shows that petitioner introduced at the hearing the following exhibits:

- 1—Mortgage dated 6/4/19.
- 2—Contract dated 6/4/19.
- 3—Petition for dissolution.
- 4—Record of dissolution.
- 5—Waiver.
- 6—Letter 12/26/23.
- 7—Letter 10/24/24 and RAR.

The respondent introduced at the hearing the following exhibits:

- A—1919 return.
- B—Assessment List 1917.
- C—Assessment List 1918.
- D—Assessment List 1919.
- E—Waiver 1917.
- F—Letter 2/7/24.
- G—Letter 6/30/24.
- H—Claim for abatement 4/16/24.
- I—Claim for abatement 4/18/24.

As will be seen from the foregoing statement of exhibits received at the hearing, the income tax return of the Bryson-Robison Corporation for 1919 was introduced in evidence as Respondent's Exhibit A, but neither the petitioner nor the respondent at any time during the hearing introduced or offered to introduce the income tax return of the corporation for 1917 and 1918. Petitioner was permitted to introduce every exhibit that he tendered at the hearing. [27]

However it is apparent from the questions and answers in the record that the income tax returns

of the corporation for 1917 and 1918 were in the custody of the counsel for respondent and were present at the hearing and we think it is a fair inference that counsel for the petitioner Bryson was under the impression that such returns were in evidence before the Board because produced at the trial by counsel for respondent. Petitioner attaches to his motion for rehearing a statement from the Collector of Internal Revenue at Tacoma, Washington, stating that the corporation returns for 1917 and 1918 were filed as follows:

The return for the year 1917 was filed on March 30, 1918.

The tentative return for the year 1918 was filed on March 14, 1919.

The complete return for 1918 was filed on June 16, 1919.

The return for the year 1919 was filed on March 15, 1920.

(2) Petitioner asks that the case be reopened for the purpose of taking additional evidence by deposition of Herbert C. Bryson, John F. Watson, Marvin Evans, and Elmer D. Bryson, upon the question of transferee liability of both petitioners, Lester L. Robison and Elmer D. Bryson, and more particularly as to whether the shares of stock owned by Lester L. Robison in the corporation were actually transferred by Robison to Bryson. In view of the testimony given by petitioner, Elmer D. Bryson himself, at the former hearing, we believe that this ground for a rehearing urged by the petitioner is

without merit. This testimony at the hearing was as follows: [28]

Q. Will you state your name, Mr. Bryson?

A. Elmer D. Bryson.

Q. Where do you live?

A. Walla Walla.

Q. What is your business?

A. Sheep raiser.

Q. Were you a member of the Bryson-Robison Corporation, the taxpayer in these cases in June of 1919?

A. Yes, sir.

Q. Did you receive some of the property that formerly had been the property of the corporation in June, of 1919?

A. I took over all of the business there.

Q. You took over all of the business?

A. Yes, sir.

Q. Will you state what the nature of that transaction was; I mean will you describe that transaction, and state what took place?

A. Well, I bought Mr. Robison's share of the business and just simply gave him \$70,000 for his half.

Q. Of the business?

A. And took it over.

Q. And then you took over the business yourself as an individual?

A. Yes, sir.

Q. Did you do that after you took over his share or at the same time or before?

A. Well we had started dissolution proceedings prior to this, but we had not finished.

Cross Examination

Q. In other words, there had not been any distribution of the property from the corporation to the individuals before that time?

A. No. [29]

Q. You just took over Mr. Robison's interest in the corporate business and assets?

A. Yes, sir, we treated it practically as a partnership business rather than a corporation and I took over everything.

Q. That was true all the way through?

A. Yes, sir.

Q. You kept no formal books and records?

A. No.

Q. But it was, in fact, a corporation?

A. Yes, it was a corporation.

Mr. Watson: That is all.

The Member: Were the assets you took over described in the deed of conveyance that has been offered here?

The Witness: The real estate was but not the personal property.

Mr. Watson: But you did take over the personal property?

The Witness: Yes, I took over everything.

The Member: That is all, Mr. Bryson.

As pointed out in our findings of fact and opinion promulgated February 26, 1931, the above testimony

of petitioner was corroborated by the witness Crow who was the attorney for the corporation who drew up the papers connected with a petition which was filed in the Superior Court for Walla Walla County to dissolve the corporation. The witness Crow testified that Robison made an actual physical transfer of his shares of stock to petitioner Bryson, but even if he is mistaken in that statement and there was no actual transfer of the physical certificate for shares of stock in the corporation, it seems clear that Robison transferred to Bryson his shares or interest in the corporation and that it was not a transfer of physical assets of the corporation by Robison [30] to Bryson. Of course if the corporation had been dissolved at the time the petition was filed with the Superior Court of Walla Walla County and the assets of the corporation had thereupon been distributed in liquidation to the two stockholders, Robison and Bryson, this transfer would make Robison as much a transferee as Bryson, but there is nothing in the record to show that the corporation was liquidated prior to Robison selling his interest and that any of the assets of the corporation were actually transferred to him. What was done—Robison sold his shares or interest in the corporation to Bryson and thereafter Bryson took charge of all of the assets and ceased to operate the corporation. Under the decisions cited in our former opinion this action clearly makes Bryson a transferee of the corporation but does not make Robison a transferee. The statute places the burden of proof on the respondent to

show transferee liability and this he failed to do in the case of petitioner Lester L. Robison. While it may be perfectly true that Bryson got decidedly the worst end of the bargain in buying out Robison, that fact does not have any bearing upon the question of transferee liability.

We therefore decline to set aside the decision entered February 26, 1931, holding Lester L. Robison not liable as transferee for any amount in respect to the tax of the Bryson-Robison Corporation for the years 1917, 1918, and 1919. [31]

(3) Petitioner Bryson asks that rehearing be granted so he can offer evidence that certain lands excluded from the invested capital of the Bryson-Robison Corporation for the taxable years 1917, 1918 and 1919 had a cost of \$55,000. The evidence shows that the respondent only excluded \$45,000 from the corporation's invested capital on account of these lands and that such exclusion was on account of the fact that the lands had been deeded prior to the taxable years by the corporation to third parties. However, at the hearing respondent amended his answer and conceded that his action in excluding these lands from the invested capital of the transferor corporation was error but respondent did not admit in his answer that the cost of the lands was \$45,000 as contended by the petitioner in his pleadings. This amended answer of the respondent put petitioner on proof of the cost of these lands and the only cost established at the hearing was \$40,000. Considerable testimony was offered

at the hearing as to the increase in value of these lands but, as pointed out in our opinion, appreciation in value of assets constituting a part of the taxpayer's invested capital does not increase invested capital. Invested capital is determined by the cost of the assets. Inasmuch as the decision of the Board awards the corporation an additional invested capital over that allowed by the Commissioner of \$40,000, which was all the cost which petitioners proved, instead of \$45,000 as excluded by the respondent, it is not believed that the proceeding should be reopened as to that issue. Petitioner's motion on that ground is accordingly denied. [32]

In view of petitioner Bryson's plea of the statute of limitations and his evident belief and understanding that the income tax returns of the Bryson-Robison Corporation for the years 1917 and 1918 were in evidence, his motion for a rehearing on that ground is granted and the proceeding is reopened for further hearing as to petitioner Bryson on the issue of the statute of limitations and is restored to the day calendar for hearing in Washington, D. C., April 29th, 1931.

(Signed) EUGENE BLACK

Member,

U. S. Board of Tax Appeals.

[Endorsed]: United States Board of Tax Appeals.
A true copy: Teste. B. D. Gamble, Clerk.

[Endorsed]: United States Board of Tax Appeals.
Enter and serve on parties. Not to be stenciled.
Mar. 25, 1931. Logan Morris, Chairman.

[Endorsed]: United States Board of Tax Appeals.
Entered Mar. 28, 1931. [33]

[Title of Court and Cause.]

Docket No. 22255.

Herbert C. Bryson, Esq., for the petitioner.

J. E. McFarland, Esq., for the respondent.

MEMORANDUM OPINION.

BLACK: Findings of Fact and opinion were promulgated in this proceeding February 26, 1931, and are reported in 22 B. T. A. 395, to which reference is hereby made.

In said report decision was made against petitioner, Elmer D. Bryson, on his plea of the statute of limitations as to all of the taxable years involved. The decision as to the taxable years 1917 and 1918 was based upon petitioner's failure to introduce any evidence as to the time of filing the income tax returns of Bryson-Robison Corporation for the taxable years 1917 and 1918. Without [34] such evidence petitioner failed to make out a prima facie case of the running of the statute of limitations and his plea of limitation could not be sustained. In a motion for a rehearing, petitioner set out what appeared to be good and sufficient reasons for his failure to offer such proof. The Board granted the motion for rehearing and has now been furnished with evidence as to the time of filing of the income tax returns of Bryson-Robison Corporation for the

years 1917 and 1918. This evidence shows that the return for 1917 was filed March 30, 1918, and therefore assessment and collection of any deficiency in the tax for 1917 from Bryson-Robison Corporation was barred by the statute of limitations on March 30, 1923, and any assessment after that date was null and void unless made under a valid waiver executed prior thereto for and on behalf of the taxpayer, Bryson-Robison Corporation.

The return of said corporation for 1918 was filed June 16, 1919, and therefore assessment and collection of any deficiency for 1918 from the transferor corporation was barred June 16, 1924, unless extended by a valid waiver. At the hearing a waiver dated January 2, 1924, covering the years 1917 and 1918 was introduced in evidence and reads as follows: [35]

INCOME AND PROFITS TAX WAIVER

In pursuance of the provisions of subdivision (d) of Section 250 of the Revenue Act of 1921, Bryson-Robison, Corporation of Walla Walla, Washington, and the Commissioner of Internal Revenue, hereby consent to a determination, assessment, and collection of the amount of income, excess-profits, or war-profits taxes due under any return made by or on behalf of the said Corporation for the years 1917 and 1918 under the Revenue Act of 1921, or under prior income, excess-profits, or war-profits tax Acts, or under Section 38 of the Act entitled "An Act to provide revenue, equalize duties, and encourage the industries of the United States, and

for other purposes'', approved August 5, 1909, irrespective of any period of limitations.

Elmer D. Bryson

Former Secretary of the Bryson-
Robison Corp.

Taxpayer.

By: D. H. Blair,

Commissioner.

If this waiver is executed on behalf of a corporation, it must be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition to which, the seal, if any, of the corporation must be affixed. [36]

Petitioner Bryson contends that this waiver is entirely ineffective to extend the period of limitations applicable to the assessment and collection of taxes for the years 1917 and 1918 against Bryson-Robison Corporation, for two reasons: (1) the corporation was dissolved July 1, 1921, and was powerless to act at the time the waiver was signed, to-wit, January 2, 1924, and the signer of the waiver, Elmer D. Bryson, had no power or authority to act for the corporation; (2) even if it be conceded that under some statute of the State of Washington the existence of the corporation was continued after the date of its dissolution for the purpose of winding up its affairs, nevertheless the waiver, on its face, taken together with the letter accompanying it, shows that it was not executed for and on behalf of the

corporation but was executed for and on behalf of Elmer D. Bryson as an individual and therefore did not have the effect of extending the statute of limitations affecting the assessment and collection of taxes against the corporation.

In support of contention (1), petitioner offered in evidence a certificate from the Secretary of State of Washington, showing the date of the dissolution of the corporation to be July 1, 1921. This certificate reads as follows: [37]

I, J. Grant Hinkle, Secretary of State of the State of Washington and custodian of the Seal of said State, do hereby certify that I have carefully examined the records of this office and find that the "BRYSON-ROBISON CORPORATION", a domestic corporation of Walla Walla, Washington, filed a copy of its articles of incorporation in this office on the 13th day of October, 1916.

I further certify that the above mentioned corporation was stricken from the records of this office July 1, 1921, and was further "Stricken from Records and dissolved" July 1, 1924 under the provisions of Chapter 144, Laws of Washington of 1923, for failure to pay the annual license fees and accruing penalties, the last license fee paid being for the fiscal year ending June 30, 1919.

And I further certify that the above mentioned corporation has had no legal corporate existence since stricken July 1, 1921, pursuant to Chapter 140, Laws of 1907.

In view of the date of the dissolution of the corporation as shown by the foregoing certificate, and the statutes with reference to dissolved corporations of the State of Washington, we think it questionable whether any one had the power to execute a waiver for the dissolved corporation on January 2, 1924 (the date the waiver in question was executed). But we feel that it is unnecessary to decide this question for the reason that, in our judgment, petitioner's contention No. (2) should be sustained. [38]

While it is true that the body of the waiver recites that the "Bryson-Robison Corporation and the Commissioner of Internal Revenue, hereby consent," etc., nevertheless the waiver is signed by Elmer D. Bryson as an individual who describes himself as the former Secretary of the Bryson-Robison Corporation, taxpayer. The waiver does not bear the seal of the corporation and moreover the waiver was transmitted to the Commissioner accompanied by a letter which strictly put the Commissioner on notice that Bryson was not executing the waiver for and on behalf of the corporation but that on the contrary he had no power to act for the corporation and was not assuming to do so. This letter reads as follows:

Commissioner of Internal Revenue,
Washington, D. C.

Sir:

Re: Your IT:CA:Ms 2506-WHS-App.

Elmer D. Bryson has handed me your office letter of the 19th inst. addressed to Bryson-

Robison Corporation, in his care, advising that it will be necessary for this corporation within twenty days from the date of your letter to advise you of its acquiescence in the determination of net income and invested capital as found by the Revenue Agent's report dated October 22, 1923, in order that you may further consider an application for computation of tax under the provisions of Section 210, Revenue Act 1917 and Sections 327-8, Revenue Act 1918. [39]

You have already been informed that this corporation has been entirely out of business since July 1919, and since that date has not owned or possessed any property of any character and the corporation has long since been stricken from the corporate rolls of this state where it was incorporated. It has not functioned in any manner since that date, and being stricken from the corporate rolls naturally the former officers of the corporation cannot legally presume to act for it since it no longer exists.

During the life of the corporation Elmer D. Bryson was secretary of the corporation, but will not presume to assume to act in that capacity after all of these years since its dissolution. The only way he could make a report would be that as that of an individual, who was formerly secretary of a corporation which has been defunct for a period of over four and one half years, and during which period it has

neither functioned nor owned any property. (underscoring supplied.)

Your office letter above referred to is being by him referred to Cosper Accounting Company, who has been looking after this matter and it will probably give your letter such further attention and reply as it deems proper and necessary. We deemed it proper that this status of affairs should now again be called to your attention, as no former officer will assume any authority not vested in him.

Yours very truly,

Herbert C. Bryson.

We think it is clear from a reading of the foregoing letter, dated December 26, 1923, that when Elmer D. Bryson executed the waiver in question and transmitted it to the Commissioner, he made it plain to the Commissioner that he was not executing it as a former officer of [40] the corporation but merely as an individual who repudiated any claim that he had authority to act for the corporation. Under these circumstances the situation is entirely different from that which existed in *Commissioner v. Godfrey*, 50 Fed. (2d) 79 and *H. D. Waldrige & Co.*, 25 B. T. A. 1109. Those were cases where the waivers in question were executed under the seals of the taxpayer corporations, and in the name of the corporations and by some one having the legal authority to act. We have, as already pointed out, an entirely different situation before us in the instant case.

The most that could be said for the waiver which we have set out above, is that it was executed by Bryson as a transferee of the assets of the original taxpayer and we have held that a waiver executed by a transferee purporting to extend the time of assessment and collection of the tax against the original taxpayer, is ineffective to extend the statute of limitations as to the original taxpayer. *Carnation Milk Products Co.*, 15 B. T. A. 566.

We therefore conclude that assessment and collection of the tax against the transferor corporation for 1917 became barred March 30, 1923, and that the assessment which the Commissioner made for 1917, on March 21, 1924, was null and void. For the same reason we hold that assessment and collection of the tax against the transferor corporation for the year 1918 was barred June 16, 1924, and that the assessment made by the Commissioner, September 1, 1925, for 1918 was likewise null and void. [41]

In our opinion promulgated in this proceeding February 26, 1931, 22 B. T. A. 395, we held that assessment and collection of the deficiency against the transferor corporation for 1919 was not barred by the statute of limitations. Petitioner Bryson in his motion for rehearing assails the correctness of this ruling but a re-examination of all the facts and a reading of the authorities cited by petitioner leaves us unconvinced of any error in our ruling as to the year 1919.

An examination of the evidence shows that the return of taxpayer corporation for 1919, was filed

March 15, 1920. Under the applicable statute of limitations, assessment and collection of the tax for 1919 would have been barred March 15, 1925, but prior thereto, to-wit, March 14, 1925, respondent assessed the asserted deficiency against the transferor corporation and this assessment* was legal. Has the statute of limitation run in favor of the petitioner, Elmer D. Bryson, as transferee against the assessment and collection from him of this \$2,973.54 assessed by the Commissioner against Bryson-Robison Corporation, March 14, 1925? We think not. This assessment was made after the enactment of the Revenue Act of 1924 and is not affected by the decision in *Russell v. United States*, 278 U. S. 181, and could have been collected from the transferor corporation within six years after the assessment, or prior to March 14, 1931.

This period of six years had not expired prior to the enactment of the Revenue Act of 1926, containing section 280 (transferee section) [42] and had not expired prior to the date of respondent's deficiency notice in this proceeding and hence we hold collection of the deficiency for 1919 was not barred under prior acts at the time such deficiency notice was mailed. *Commissioner v. Jonathan Godfrey*, *supra*.

Petitioner further contends that the assessment of the 1919 deficiency made by the Commissioner of Internal Revenue, March 14, 1925, against the Bryson-Robison Corporation was a nullity because proper notice was not given thereof. We think this contention is without merit. Respondent introduced

in evidence a document entitled, "Assessment List, District of Washington. Month March Special #7, year 1925. Additional assessment made by Commissioner. Personals \$136,336.01, corporations \$50,-878.17." Included in the additional assessments made against corporations was \$2,973.54 against Bryson-Robison Corporation, Walla Walla, Washington, and attached to the assessment list is this certificate: "I hereby certify that I have made inquiries, determinations and assessment of taxes, penalties, etc. of the above classification specified in these lists, and find that the amounts of taxes, penalties, etc. stated as corrected and as specified in the supplementary pages of this list made by me, are due from the individuals, firms, and corporations opposite whose names such amounts are placed, and that the amount chargeable to the collector is as above. Dated at Washington, D. C. Office of Commissioner of Internal Revenue, March 14, 1925." [43]

We think this evidence, above quoted, discloses a legal assessment of the deficiency for 1919 and we therefore overrule petitioner's assignment of error which attacks its validity.

Petitioner Bryson also strongly urges in his brief that we permit an amendment to his petition to conform to the proof; admit and consider petitioner's exhibit #7 which he claims conclusively establishes a complete settlement between Bryson-Robison Corporation and Elmer D. Bryson on the one hand and the Commissioner of Internal Revenue on the other hand, and that by reason thereof we hold that there is no deficiency for 1919. Petitioner's exhibit #7

was admitted in evidence and is before us for consideration, and if it showed a valid closing agreement for the year 1919, as defined by the statute, we would find that there was no deficiency for 1919. But the exhibit to which petitioner refers does not evidence a closing agreement as defined by statute.

Exhibit #7 is the report of an internal revenue agent covering the years 1919, 1920 and 1921, of the taxes of Elmer D. Bryson as an individual. It does not purport to deal in any respect with the liability of Elmer D. Bryson as the transferee of the assets of the Bryson-Robison Corporation. The proceeding which we are now considering deals with the liability of petitioner, Bryson, as a transferee of the assets of Bryson-Robison Corporation and with nothing else. This revenue agent's report (Petitioner's exhibit #7) agreed [44] to by Bryson, could not be considered in any respect as a closing agreement affecting Bryson's liability as a transferee of the assets of Bryson-Robison Corporation. Therefore it would not affect in any way the questions which we have to decide in this proceeding. However, in view of petitioner Bryson's insistence in his brief, we point out that even as to Bryson's individual tax liability, the document in question does not evidence a closing agreement as defined by statute.

Section 1006, Revenue Act of 1924, which governs the alleged closing agreement because it is dated in 1924, defines a closing agreement as follows:

If after a determination and assessment in any case the taxpayer has paid in whole any tax or penalty, or accepted any abatement, credit, or re-

fund based on such determination and assessment, and an agreement is made in writing between the taxpayer and the Commissioner, with the approval of the Secretary, that such determination and assessment shall be final and conclusive, then (except upon a showing of fraud or malfeasance or misrepresentation of fact materially affecting the determination or assessment thus made) (1) the case shall not be reopened or the determination and assessment modified by any officer, employee, or agent of the United States, and (2) no suit, action or proceeding to annul, modify, or set aside such determination or assessment shall be entertained by any court of the United States. (Underscoring supplied.)

Petitioner has not shown any closing agreement assented to by the Secretary of the Treasury and his plea in that respect thereto is therefore denied. *Stein-Bloch Co.*, 23 B. T. A. 1162; *Botany Worsted Mills*, 278 U. S. 282. [45]

Decision will be entered that petitioner, Elmer D. Bryson, is not liable for any deficiency of Bryson-Robison Corporation for the years 1917-1918.

Decision will be entered that petitioner, Elmer D. Bryson, is liable for deficiency of Bryson-Robison Corporation for the year 1919, plus interest thereon as provided by law and said deficiency for 1919 will be redetermined in accordance with our findings of fact and opinion promulgated February 26, 1931, and

Enter:

[Endorsed]: Entered Jul. 20, 1932.

[Title of Court and Cause.]

Docket No. 22255.

ORDER.

The Board having promulgated its Opinion in the above entitled proceeding on February 26, 1931, and having entered its Memorandum Opinion therein on July 20, 1932, sustaining its Opinion of February 26, 1931, respecting the taxable year 1919, but holding that liability for 1917 and 1918 taxes was barred by the Statute of Limitations, the respondent filed herein on August 22, 1932, a motion for reconsideration and review of said Memorandum Opinion entered July 20, 1932. Respondent in support of his said motion filed a memorandum brief which has been carefully considered and all the authorities cited read and studied. It is not believed that respondent's said motion should be granted. On authority of *Barron-Anderson Company v. Commissioner*, 17 B. T. A. 686 and *Newport Company*, 22 B. T. A. 833, we hold that assessment and collection of the tax against the transferor corporation was barred by the Statute of Limitations prior to the enactment of the Revenue Act of 1926. Therefore, since assessment and collection of the liability of the transferor corporation were barred prior to passage of the Revenue Act of 1926, assessment and collection of the liability of the petitioner, as transferee, are also barred. *Caroline J. Shaw, Executrix*, 21 B. T. A. 400; *E. N. Ennis and others*, 21 B. T. A. 406. [47]

ORDERED; That said motion be and the same is hereby denied.

[Seal] (Signed) EUGENE BLACK,
Member, United States Board of
Tax Appeals.

[Endorsed]: Entered Sep. 22, 1932. [48]

United States Board of Tax Appeals.

Docket No. 22255

ELMER D. BRYSON,

Petitioner,

vs

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION.

On October 31, 1932, respondent filed in this proceeding a proposed determination of tax liability of petitioner, Elmer D. Bryson, as transferee of the assets of Bryson-Robison Corporation, under Rule 50, in accordance with the findings of fact and opinion promulgated by the Board, February 26, 1931, as modified by the memorandum opinion entered July 20, 1932. Said proposed determination filed by respondent was set for hearing under Rule 50 for January 4, 1933. Prior to said date petitioner filed objections to the determination of tax liability which had been filed by respondent. In said objections petitioner makes a computation of his own

based on an alleged error made by respondent in the inventory of lambs.

Petitioner alleges that on page 3 of Exhibit 7, which is a report of the Revenue Agent which was approved and acted upon by respondent, under the heading "Inventory 12th month, 31st day, 1919", an item of 100 lambs at \$8.15 each is carried in the inventory at a total of \$8,150. Following is a statement of this inventory as shown on page 3 of the Revenue Agent's report:

Inventories 12-31-19

1500 Ewes at \$4.00	\$ 6,000.00	
1700 Sheep at 8.91	15,147.00	
100 Lambs at 8.15	8,150.00	
Cattle	1,925.00	
	<hr/>	
Total closing inventories		31,222.00
		<hr/>

[49]

Petitioner claims that this inventory item should be reduced \$7,235 and that thus reduced it will affect the tax liability of the corporation in the amount shown in petitioner's computation. The discrepancy which petitioner points out in his said objection is manifestly a typographical error. An inspection of the item shows that it is plain that the inventoried item is 1,000 lambs at \$8.15 each instead of 100 lambs at \$8.15 each. That such discrepancy was plainly a typographical error is shown by an examination of page 21 of the same Revenue Agent's report on

which is shown the following statement as to inventories:

(b) Inventories increased by \$577.00 to agree with the corrected inventory shown in the report of the corporation as follows:

Old Inventory 1919		
1500 Ewes	at \$10.00	\$15,000.00
200 lambs	" 12.50	2,500.00
700 "	" 3.30	2,310.00
800 "	4.45	3,560.00
1000 "	5.35	5,350.00
Total		\$28,720.00

Revised inventory 1919 based on purchases
by the Walla Walla Meat & Cold Storage Co.

1500 ewes at	\$4.00	6,000.00
1700 sheep "	8.91	15,147.00
1000 lambs "	8.15	8,150.00
Total		\$29,297.00

We find no merit in petitioner's said objections, all of which have been carefully examined. We find the computation submitted by respondent is in accordance with the findings of fact and opinion of the Board promulgated February 26, 1931, as modified by the Board's memorandum opinion entered, July 20, 1932. Wherefore, premises considered, it is:

ORDERED AND DECIDED that petitioner, Elmer D. Bryson, is not liable for any deficiency of the Bryson-Robison Corporation for the year 1917 and 1918 because we have held that all such liability

is barred by the applicable statutes of limitation. Petitioner, Elmer D. Bryson, is liable as transferee of the assets of the Bryson-Robison Corporation for deficiency due for said corporation for the year 1919 to the amount of \$2,273.54, together with interest thereon as provided by law.

[Seal]

(Signed) EUGENE BLACK,
Member, U. S. Board of Tax Appeals.

Entered: Jan. 26, 1933. [50]

[Title of Court and Cause.]

B.T.A. Docket No. 22,255

PETITION FOR REVIEW AND
ASSIGNMENTS OF ERROR.

To the Honorable Judges of the United States
Circuit Court of Appeals for the Ninth Circuit:
NOW COMES David Burnet, Commissioner of
Internal Revenue, by his attorneys, Sewall Key,
Special Assistant to the Attorney General; C. M.
Charest, General Counsel, Bureau of Internal Revenue,
and Elden McFarland, Special Attorney, Bureau of
Internal Revenue, and respectfully shows:

I.

The petitioner for review is the duly appointed, qualified and acting Commissioner of Internal Revenue of the United States, holding office by virtue of the laws of the United States. The respondent is an individual, an inhabitant of the Ninth Judicial Circuit of the United States, residing at Walla

Walla in the State of Washington. The income and profits tax returns of Bryson-Robinson Corporation for the years 1917 and 1918 were filed with the Collector of Internal Revenue for the collection District of Washington, which said collection district lies within the Ninth Judicial Circuit. [51]

II.

The petitioner determined a deficiency in income and profits taxes of Bryson-Robison Corporation for the calendar year 1917 in the amount of \$2,863.42 and for the calendar year 1918 in the amount of \$5,741.89; and on November 3, 1926, in accordance with the provisions of sub-division (a) (1) of Section 280 and of sub-division (a) of Section 283, Revenue Act of 1926, sent to respondent by registered mail a notice of said deficiencies, proposing to assess them against respondent as transferee of the property of Bryson-Robison Corporation. Thereafter, respondent duly filed with the United States Board of Tax Appeals his petition for redetermination of the deficiencies proposed in the notice of deficiency. The matter was heard by the Board of Tax Appeals on June 2, 1930. On February 26, 1931 the Board promulgated its interlocutory decision (reported at 22 B. T. A. 395), a second interlocutory decision (unreported) on March 28, 1931, a third interlocutory decision (unreported) on July 20, 1932, a fourth interlocutory decision on September 22, 1932 (unreported) and on January 26, 1933, entered its final decision and order of redetermination wherein it ordered and decided that respondent was

not liable for the deficiencies in income and profits taxes due from Bryson-Robison Corporation for the years 1917 and 1918 because his liability was barred by the statute of limitations.

III.

During the entire calendar years 1917 and 1918, Bryson-Robison Corporation was a corporation organized and existing under the laws of the State of Washington and was engaged in the business of raising sheep in the State of Washington. Respondent and Mr. Robison each owned one-half of the capital stock of the corporation. In June, 1919, Mr. Robison sold [52] his capital stock to Mr. Bryson for \$70,000.00. Mr. Bryson then caused all of the assets to the corporation to be transferred to himself; and as an individual he continued to conduct the business theretofore carried on by the corporation. The income and profits tax return of the corporation for the year 1917 was filed with the Collector of Internal Revenue at Tacoma, Washington, March 30, 1918, and that for the year 1918 was filed June 16, 1919. The annual corporation license fees required by the laws of Washington were paid for the corporation for the fiscal year ended June 30, 1919 but were not paid for subsequent years; and pursuant to the provisions of those laws the corporation was stricken from the rolls of the Secretary of State of Washington, July 1, 1921 and again on July 1, 1924.

On February 12, 1923 respondent executed a waiver whereby he, Elmer D. Bryson, consented to

the extension of the time within which determination, assessment and collection of the income and profits taxes of Bryson-Robison Corporation, might be made, for the period of one year from that date. An investigation and examination of the tax liability of the corporation was made by an agent of the Bureau of Internal Revenue. As a result of that examination petitioner notified respondent that additional taxes were due for the years 1917, 1918 and 1919 from the corporation. The respondent requested that the proposed taxes be reduced under the special assessment provisions of the Revenue Acts (Section 210, Revenue Act of 1917 and Sections 327 and 328 of the Revenue Act of 1918). In a letter dated December 19, 1923, petitioner replied that it would be necessary for the corporation to acquiesce in the Revenue Agent's report in order that the application for special assessment might be further considered.

Respondent replied by letter dated December 26, 1923, stating that inasmuch [53], as the corporation had been stricken from the corporate rolls and no longer existed, he could not legally presume to act either for the corporation or as secretary for the corporation, and that the only way he could make a report would be as an individual, who was formerly secretary of the defunct corporation. He further stated that the letter of December 19 was being referred to certain accountants who would give the letter such further attention and reply as was deemed proper and necessary.

With the letter of December 26, 1923, respondent enclosed a waiver dated January 2, 1924 signed "Elmer D. Bryson, former Sec'y of the Bryson-Robison Corporation, taxpayer", stating that Bryson-Robison Corporation consented to the determination, assessment and collection of its income and profits taxes for the years 1917 and 1918, irrespective of any period of limitations.

On February 7, 1924 and in further reply to petitioner's letter of December 19, 1923, respondent filed with the petitioner a protest against the proposed assessment of additional taxes for the years 1917 and 1918, against the corporation, signing the protest "Bryson-Robison Corporation, by Elmer D. Bryson, formerly Sec."

Additional taxes for the year 1917 in the amount of \$5,896.86 were assessed against the corporation March 21, 1924. In April, 1924, respondent filed two claims for abatement of the additional taxes assessed against the corporation for 1917, signing both claims "Elmer D. Bryson, formerly Secretary of Bryson-Robison Corporation"; and in June 30 he filed another protest signed "Bryson-Robison Corporation, Elmer D. Bryson, formerly Secretary."

The proposed additional taxes for the year 1918 in the amount of [54] \$5,741.89 were assessed against in corporation September 1, 1925. On September 18, 1925, the Commissioner signed a schedule allowing in part the claims in abatement for the year 1917, abating \$3,033.44 of the additional assessment and denying the claim as to \$2,863.42. The petitioner's final determination and denial of respondent's protests

was contained in the notice of deficiency mailed to respondent November 3, 1926, proposing to assert the corporation's liability against respondent as transferee of the corporation's property. Respondent thereupon filed his petition for re-determination with the United States Board of Tax Appeals. The Board held that respondent's liability in respect of the taxes due from the corporation for the years 1917 and 1918, was barred by the statute of limitations.

IV.

The nature of the controversy is such as to give rise to four questions:

1. Did the Bryson-Robison Corporation and the Commissioner of Internal Revenue consent in writing to extend the period of time within which assessment and collection of the income and profits taxes of Bryson-Robison Corporation for the years 1917 and 1918 might be made?

2. Did the respondent and the Commissioner of Internal Revenue consent in writing to extend the period of time within which assessment and collection of the income and profits taxes of Bryson-Robison Corporation for the years 1917 and 1918 might be made?

3. Does the execution of a waiver by a transferee of all the assets of a dissolved corporation, purporting to extend the time of assessment and collection of taxes against the corporation, extend the period of limitation for assessment and collection as to the transferee? [55]

4. Where, by reason of his execution of two waivers, the transferee of all of the assets of a dissolved corporation who also was the sole stockholder of the corporation at the time of its dissolution, has secured to himself the benefits (1) of a postponement of the assessment and collection of the taxes of the dissolved corporation beyond the statutory period for such assessment or collection except as extended by such waivers, (2) a consideration of his application for special assessment under the provisions of Section 210, Revenue Act of 1917, and Sections 327 and 328 of the Revenue Act of 1918; and (3) a consideration of his claim in abatement whereby a major portion of the additional tax assessed against the corporation for the year 1917 eventually was abated, is he estopped to deny the validity of the waivers?

V.

The petitioner desires to obtain a review of the aforementioned decisions of the United States Board of Tax Appeals by this Honorable Court.

VI.

The petitioner says that in the record and proceedings before the United States Board of Tax Appeals and in the decisions and order of redetermination promulgated and entered by the Board, manifest error occurred, and upon which he relies to reverse the said decisions and order of redetermination so promulgated and entered by the Board, to wit:

1. The Board erred in holding that the March, 1924, assessment against Bryson-Robison Corporation of the additional income and profits taxes for the year 1917, was barred by the statute of limitations.

2. The Board erred in holding that the September, 1925, assessment of additional income and profits taxes for the year 1918 against Bryson-Robison Corporation was barred by the statute of limitations. [56]

3. The Board erred in holding that the assessment and collection of the income and profits taxes due from Bryson-Robison Corporation, against respondent as a transferee of the property of that corporation was barred, by the statute of limitations.

4. The Board erred in holding that the waivers executed by the transferee of all of the assets of the original taxpayer purporting to extend the time of assessment and collection against the original taxpayer were ineffective to extend the statute of limitations either as to the original taxpayer or as to the transferee.

5. The Board erred in holding that the waiver of February 12, 1923 did not extend the period of time within which assessment and collection of the income and profits taxes of Bryson-Robison Corporation might be made.

6. The Board erred in failing to hold that the waiver of January 2, 1924 was executed for and on behalf of the Bryson-Robison Corporation.

7. The Board erred in failing to hold that respondent did have authority to execute the waiver

of January 2, 1924 on behalf of the taxpayer corporation.

8. The Board erred in holding that the assessment and collection of the tax against the corporation for the year 1917 became barred March 30, 1923.

9. The Board erred in holding that the assessment and collection of the tax against the corporation for the year 1918 became barred June 16, 1924.

10. The Board erred in holding that the assessment against Bryson-Robison Corporation for the year 1917, made March 21, 1924, was null and void.
[57]

11. The Board erred in holding that the assessment against the corporation for the year 1918, made September 1, 1925, was null and void.

12. The Board erred in failing to find that by reason of his execution of the waivers of February 12, 1923 and January 2, 1924, respondent secured a postponement to a time beyond the period of limitation except as extended by said waivers, of the assessment and collection of additional income and profits taxes due from Bryson-Robison Corporation for the years 1917 and 1918.

13. The Board erred in failing to find that by reason of his execution of the waivers of February 12, 1923 and January 2, 1924, respondent secured a consideration of his application for special assessment of the income and profits taxes of Bryson-Robison Corporation for the years 1917 and 1918, under the provisions of Section 210, Revenue Act of 1917, and Sections 327 and 328 of the Revenue Act of 1918.

14. The Board erred in failing to find that by reason of his execution of the waivers of February 12, 1923 and January 2, 1924, respondent secured consideration of his claims for abatement of the additional income and profits taxes assessed against Bryson-Robison Corporation for the year 1917, and secured an allowance of said claims to the extent of \$3,033.44.

15. The Board erred in failing to hold that respondent was estopped to deny the validity of the waivers of February 12, 1923 and January 2, 1924.

WHEREFORE, the Commissioner petitions that the decision of the Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals for the Ninth Circuit, that a transcript of the record be prepared in accordance with law and with the rules of said Court and transmitted to the [58] clerk of said Court for filing, and that appropriate action be taken to the end that the errors complained of may be reviewed and corrected by said Court.

(Sgd.) SEWALL KEY

Special Assistant to the
Attorney General.

(Sgd.) C. M. CHAREST

General Counsel,
Bureau of Internal Revenue.

Of Counsel:

(Sgd.) ELDEN McFARLAND

Special Attorney,
Bureau of Internal Revenue.

United States of America,
District of Columbia—ss.

C. M. Charest, being duly sworn, says that he is General Counsel of the Bureau of Internal Revenue, and as such is duly authorized to verify the foregoing petition for review; that he has read said petition and is familiar with the contents thereof; that said petition is true of his own knowledge except as to the matters therein alleged on information and belief, and as to those matters he believes it to be true.

(Sgd.) C. M. CHAREST

Subscribed and sworn to before me this 19 day
of April, A. D. 1933.

(Sgd.) MARCELLETE M. TAYLOR
Notary Public.

My commission expires Mar. 31, 1935.

[Endorsed]: United States Board of Tax Appeals.
Filed Apr. 19, 1933. [59]

[Title of Court and Cause.]

Docket No. 22,255

NOTICE OF FILING PETITION FOR
REVIEW.

To:

Herbert C. Bryson, Esq.,
312-13 Drumheller Bldg.,
Walla Walla, Washington.

You are hereby notified that the Commissioner of
Internal Revenue did, on the 19th day of April,

1933, file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Ninth Circuit, of the decision of the Board heretofore rendered in the above-entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated this 19th day of April, 1933.

(Sgd.) C. M. CHAREST,

General Counsel, Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of errors mentioned therein, is hereby acknowledged this 25 day of April, 1933.

(Sgd) HERBERT C. BRYSON,

Attorney for respondent on review.

[Endorsed]: United States Board of Tax Appeals.
Filed May 4, 1933. [60]

[Title of Court and Cause.]

Docket No. 22,255

NOTICE OF FILING PETITION
FOR REVIEW.

To:

Mr. Elmer D. Bryson,
605 Boyer Avenue,
Walla Walla, Washington.

You are hereby notified that the Commissioner of Internal Revenue did, on the 19th day of April, 1933,

file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Ninth Circuit, of the decision of the Board heretofore rendered in the above-entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated this 19th day of April, 1933.

(Sgd.) C. M. CHAREST,

General Counsel, Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of errors mentioned therein, is hereby acknowledged this 25 day of April, 1933.

(Sgd) ELMER D. BRYSON,

Respondent on Review.

[Endorsed]: United States Board of Tax Appeals. Filed May 4, 1934. [61]

[Title of Court and Cause.]

B. T. A. Docket No. 22,255

STATEMENT OF EVIDENCE.

The following is a statement of evidence in narrative form in the above-entitled cause. This cause came on for hearing before the Honorable Eugene Black, Member of the United States Board of Tax Appeals, on June 2, 1930, at Spokane, Washington. Herbert C. Bryson, Esq., appeared for the respondent on review and C. M. Charest, General Counsel,

Bureau of Internal Revenue, and Elden McFarland, Special Attorney, Bureau of Internal Revenue, appeared for the petitioner on review. The cause was consolidated for hearing with another then pending before the United States Board of Tax Appeals, entitled Lester L. Robison, petitioner, v. Commissioner of Internal Revenue, and numbered Docket No. 22,184 and in which John F. Watson, Esq., appeared for petitioner Robison.

Petitioner on review offered in evidence the income and profits tax return of Bryson-Robison Corporation for the calendar year 1919. The return was received in evidence and was marked Exhibit "A".

Petitioner on review then offered in evidence certified copies of the assessment lists assessing additional income and profits taxes against the Bryson-Robison Corporation for the years 1917, 1918 and 1919, respectively. They were received in evidence and were marked Exhibits "B", "C" and "D", respectively. [62]

Petitioner on review then called

W. R. LARSON

as a witness who, first having been duly sworn, testified as follows:

Redirect Examination.

My name is Wallace R. Larson and my official position is that of Deputy Collector of Internal Revenue. As such Deputy Collector of Internal Revenue I have examined the records of the Collector of Internal Revenue at Tacoma and particularly the records of the account of the Bryson-

(Testimony of W. R. Larson.)

Robison Corporation in that office for the calendar years 1917, 1918 and 1919. I believe that the assessment certificates that have been received in evidence as Exhibits "B", "C" and "D" are the ones that I have examined. The additional tax assessed as shown by those assessment certificates have not been satisfied. The only difference is in part of it, part of one of these has been abated. That is Exhibit "B". Part of the additional tax set up for the year 1917, the total amount set up was \$5,896.86, and this additional tax set up, and of that amount, \$3,033.44 was abated, credited against the account, leaving a balance of \$2,863.42 for that year.

There was no cross-examination and the witness was excused.

LESTER L. ROBISON

was called as a witness for and on behalf of the petitioner on review, and after having been duly sworn was examined and testified as follows:

Direct Examination.

My name is Lester L. Robison and I live at Walla Walla. My business is that of farmer and stockman. I am the petitioner in one of these cases. I was a member of the corporation known as the Bryson-Robison Corporation, the taxpayer in this case. I was a member of that corporation prior to June, 1919. Mr. Bryson and myself were the stockholders of that corporation. The approximate holding of each, that is the proportion each of us owned in the corporation was one-half. Sometime in June, 1919, I sold out to Mr. Bryson for the sum of \$70,000.00.

(Testimony of Lester L. Robison.)

Mr. Bryson took the [63] assets of the corporation and has been holding them ever since. The corporation had no assets after that time,—the time I sold out to Mr. Bryson and the corporation has no assets now.

By Mr. McFarland:

“Q. How about the liabilities of the corporation, were they very much at the time of the transfer of those assets?

“A. I do not know of any other than just Mr. Bryson gave me, to take care of the liabilities.

“Q. He gave you what?

“A. He gave me \$70,000; he was to take care of what liabilities we had.

* * * * *

“Q. Did you sell your interest in the corporation to Mr. Bryson or did the corporation transfer the assets to you and Mr. Bryson and then you sold?

“A. No, I sold to Mr. Bryson, * * * and he took the assets of the corporation; that is the way it was.”

Cross Examination.

(By Mr. Watson):

I transferred to Mr. Bryson my interest in the corporation, and its property and I joined the corporation in conveyancing to Mr. Bryson. He (Mr. Bryson) paid \$70,000.00 for that to me. Some of

(Testimony of Lester L. Robison.)

the assets of the corporation were transferred to me before I transferred to Mr. Bryson. In this transaction there was a transfer from the corporation to Mr. Bryson. I think, but I do not hardly remember, that the assets that went to Mr. Bryson never went through me but from the corporation to him. He paid me for my interest but I do not remember just exactly how the assets were handled. My wife had one share of stock. I think Mrs. Bryson had a share of stock too. I held four hundred and ninety-nine shares and Mrs. Robinson one. I do not remember whether Mr. Herbert Bryson had any of [64] the stock or not. After this transfer to Mr. Bryson I had nothing to do with the corporation; I quit immediately. I did not attend any corporate meetings or undertake to represent the corporation in any way. In other words, I severed all connection with the corporation and its business and assets. I considered I was out of it.

“THE MEMBER: Mr. Robison was this transfer evidenced by an instrument in writing, this transaction between you and Mr. Bryson?

“THE WITNESS: Yes, I got—there was an agreement between us but I have not the agreement; I have lost it.

“THE MEMBER: You do not have it with you?

“THE WITNESS: No, I have not had it for some time. When this came up I tried to find it, but I have never been able to find it.”

(Testimony of Lester L. Robison.)

The respondent on review then offered in evidence a certified copy of the conveyance made to Mr. Bryson, signed by the Bryson-Robison Corporation and by L. L. Robison and his wife. Also a certified copy of the mortgage for \$70,000.00 payable to L. L. Robison who is Lester L. Robison, covering the property that is involved and signed by the petitioner Bryson and his wife. These were received in evidence as Exhibits 1 and 2.

ELMER D. BRYSON

was called as a witness for and on behalf of the petitioner on review and after having been first duly sworn, was examined and testified as follows:

Direct Examination

My name is Elmer D. Bryson and I live at Walla Walla. My business is that of sheep raiser. I was a member of the Bryson-Robison Corporation, the taxpayer in these cases, in June of 1919. In June, 1919, I took over all of the business. I bought Mr. Robison's share in the business and [65] just simply gave him \$70,000.00 for his half of the business and then I took over the business myself as an individual. We had started dissolution proceedings prior to this but had not finished.

Cross Examination.

(By Mr. Watson):

There had not been any distribution of the prop-

(Testimony of Elmer D. Bryson.)

erty from the corporation to the individuals before that time. I just took over Mr. Robison's interest in the corporate business and assets. We treated it practically as a partnership business rather than a corporation. We kept no formal books and records, but it was, in fact, a corporation.

“THE MEMBER: Were the assets you took over personally described in the deed of conveyance that has been offered here?”

“THE WITNESS: The real estate was but not the personal property.

“MR. WATSON: But you did take over the personal property?”

“THE WITNESS: Yes, I took over everything.”

The witness was then excused.

Thereupon the respondent on review, to maintain the material averments of their petition, introduced the following proof:

W. F. CROWE,

was called as a witness for and on behalf of the respondent on review and after first being duly sworn was examined and testified as follows:

Direct Examination.

(By Mr. Watson):

My name is W. F. Crowe and I am an attorney at Walla Walla, Washington, and have been at all times during the past ten years or more, or since 1898. I was an attorney for the Bryson-Robison

(Testimony of W. F. Crowe.)

Corporation at all times I believe after it was formed, and while, early in 1917 when it had trouble with the Forest Reserve at the time, and I looked after its income tax and business [66] from that time on to its disincorporation and brought suit for its dissolution. The transfer of the business of the corporation—the transfer of June, 1919—was originally made pro forma in order to comply with Government Regulations. There is some information as a matter of record, because they were never reconveyed; that is, they were reconveyed to the corporation, but the reconveyance was never placed of record so that the apparent record title to the property was in Mr. Robison instead of in the corporation. That is as to part of property, half of the property and too, the transfer as originally made was not merely of the land but of the sheep and all of the assets, but they continued to keep them by the corporation, to treat them as the corporation's property and make their income taxes and raise income and they are the expenses from the corporation. All of the checks of the corporation passed through my hands ultimately after they had been paid for income tax. The real owner was functioning at the time of the Bryson-Robison deal and at the time of the deal before the transfer was actually made the resolutions were adopted. I have the date of it at the time, and I can refresh my memory. On April 22nd, 1919, resolutions to disincorporate were adopted, when the deal was closed. The assets and

(Testimony of W. F. Crowe.)

business were transferred from the corporation to Elmer D. Bryson, including Mr. Robison's stock, which was indorsed and turned over, also the stock of his wife.

(By Mr. Bryson, attorney for the respondent on review):

"Q. Mr. Crowe, you were in charge of the dissolution proceedings?

"A. Yes, sir.

"Q. Aren't you mistaken as to the actual corporate stock certificates being assigned and transferred?

"A. Of course, I would not remember, just without referring to notes whether they actually had or not, but I prepared affidavits at that time showing that they were actually transferred."

[67]

I started the dissolution proceedings of the corporation having for its purpose the dissolution of this corporation at that time. The occasion for transferring the corporate stock when the corporation was dissolved was so that if any assets were in the hands of the corporation instead of being distributed to Mr. Robison, they were distributed to Mr. Bryson pursuant to his purchase. I think I prepared those dates. I do not believe the bill was actually made in my presence, but the assets were not merely those known, but all of the assets of the corporation. I base this upon the memorandum Mr. Bryson prepared and filed in the Revenue Department at that

(Testimony of W. F. Crowe.)

time and certain affidavits that he was the owner of all of the stock and all the assets. The whole object and purpose of all of this transaction was that Mr. Robison sell his interest in the Bryson-Robison Corporation and all of his assets and that Elmer D. Bryson purchase them for a price or consideration of \$70,000.00 which was to be evidenced by a real estate mortgage. The deed was given by the corporation and Lester L. Robison and wife to Elmer D. Bryson, conveying all of the corporate real estate, and there was the transfer of all of the personal property of the corporation to Elmer D. Bryson. Elmer D. Bryson executed a mortgage for \$70,000 and I was then and there instructed to dissolve the corporation. At that time I started dissolution and Mr. Bryson undertook the expense of dissolution.

(At this point there was introduced in evidence what purported to be certified copies of the dissolution proceedings in the Superior Court of Walla Walla County, Washington. Said document so offered was received in evidence and marked Exhibit No. 3)

Direct Examination continued by Mr. Watson, attorney for respondent on review: [68]

I think I have already explained why Mr. Robison and his wife joined the corporation in this deed to Mr. Bryson. The record title to part of the land stood in the name of Lester L. Robison, and through a former deed made from the corporation to him in 1917, in the fall of 1917. I think that on June 4,

(Testimony of W. F. Crowe.)

1919 I had in my possession a deed from Mr. Robison and his wife conveying back to the corporation all of his property.

(Direct Examination by Mr. Bryson, attorney for respondent on review):

“Q. But there was other corporation real estate aside from that covered by this deed from Bryson and Robison and wife, back to the corporation which stood in the name of the corporation was there not?”

It is possible that some small tracts might have been acquired. Half of the real estate that had been owned or stood of record in the name of Mr. Bryson, but the corporation deed ran not only to that land which stood in his name, not only that land which stood in the name of Mr. Robison, but ran also to the land which stood in the name of Mr. Bryson and was a confirmation to that extent. After this deed of March 4, 1917, the corporation acquired some 2,000 or 2,400 acres of land, title of which was taken in the name of the corporation itself and stood in the name of the corporation itself at the time of this deed too. The deed that the corporation made covered all of the land if I remember correctly, that belonged to the Bryson-Robison Corporation, either at its beginning or afterwards, acquired up to the time of dissolution.

(Testimony of W. F. Crowe.)

By Mr. McFarland, attorney for petitioner on review:

“I would like to make an objection. The witness says that this included all of the land that was owned by the corporation up to its dissolution. Now, that assumes a fact which is not in evidence, that is that the dissolution occurred at a time prior to the time of the deed, which I think is not the case.”

The WITNESS: No, that would bear the wrong inference, and if I so stated I would like to correct my testimony. [69]

“Mr. McFARLAND: That is the only point I make on that.”

The witness continuing stated: It included all of the land which was involved in the reconveyance by the corporation to the individual stockholders for the purpose of complying with the permit regulation in the Forest Reserve of land which it afterwards acquired. That is, after the passing of this resolution any further lands were acquired in the name of the corporation so that it actually did include all. I did not intend to say that the corporation did not acquire in the corporate name deed to any real estate in the corporate name after the date of this deed from the Bryson-Robison Corporation to Mr. Bryson and Mr. Robison. I stated that all they acquired after that date was also included in the corporation deed.

(Testimony of W. F. Crowe.)

Cross Examination.

(By Mr. McFarland):

The matter of the final dissolution was in order for hearing at any time for Mr. Bryson's convenience, the order of dissolution could be entered at the time and I told him what the expenses involved with the final closing of the case would be and the matter was not particularly dropped. The corporation just became dissolved by operation of law, by his failure to come in and make the necessary showing to the Court which could have been done. I think Exhibit 3 is the entire final record in the case. I have a copy of everything filed in the Court and I have my case file before me. There is in it no order of dissolution.

(At this point there was offered in evidence the official certificate from the Secretary of State of the State of Washington, under the seal of his office concerning the dissolution of the Bryson-Robison Corporation. This document was received in evidence and marked Exhibit No. 4). [70]

ELMER D. BRYSON,

was called as a witness for and on behalf of the respondent on review and having been first duly sworn was examined and testified as follows:

Direct Examination.

By Mr. Bryson (counsel for respondent on review):

“Q. You were an officer of the Bryson-Robison Corporation through its corporate existence,

(Testimony of Elmer D. Bryson.)

were you not?

“A. Yes, sir.

“Q. I will ask you if at any time, acting for yourself or with authority of the corporation you have ever signed any waiver of assessment or distraint or collection as internal revenue for the corporation?

“A. I signed a waiver with the express understanding I had no authority to sign.

* * * * *

Mr. BRYSON: I will now ask counsel for the Commissioner to produce the waiver that is referred to by the witness in the present testimony.

By Mr. Bryson:

“Q. I will ask you to examine this document captioned income tax and profits tax waiver and ask you if that is your signature?

“A. It is.”

(At this point there was offered in evidence the said waiver which was received in evidence and marked Exhibit No. 5).

At the time I executed this waiver I had no authority from the Bryson-Robison Corporation to execute such waiver. I did not discuss the execution of this or any waiver with Mr. Robison or with any other stockholder of the Bryson-Robison Corporation at the time I signed this. At the time of signing the waiver I informed the Commissioner of Internal Revenue as to my lack of authority to

(Testimony of Elmer D. Bryson.)

sign it. That notice was contained in writing in a letter. [71]

(At this point the letter which accompanied the waiver to the Commissioner was offered and received in evidence and marked Exhibit 6.)

I have never signed any waiver of assessment or collection or distraint for the collection of income taxes in my own behalf for the years 1917, 1918 or 1919. The only record or knowledge of any assessment of tax ever having been served upon me personally as a transferee of the Bryson-Robison Corporation prior to the institution of this proceeding before this Board is that notice. I do not know whether you would call that really an assessment or not. That was November 3, 1926, at the time we started this proceeding. That is the first I have any memory of that was served on me personally. That was the first demand made on me as transferee. As I understand an assessment I have no record or memory of any assessment against the Bryson-Robison Corporation having been served upon me as an officer of the corporation. To my knowledge I never received anything as an officer of the corporation or individually from the Commissioner of Internal Revenue or any of its officers or agents of the purport and character of Exhibits B, C, and D. I never received anything of that sort for either the years 1917, 1918 or 1919, either in my personal capacity or as an officer of the corporation.

By Mr. Bryson:

“Q. Have you ever received any notice of as-

(Testimony of Elmer D. Bryson.)

assessment as transferee of the Bryson-Robison Corporation until this notice of November 3, 1926, on which this action is predicated?

“A. Notice to apply for hearing before the Appeal Board; I do not know whether it is an assessment.

“Q. Well, that is the notice on which this action is based.

“A. That is the only one; I remember that.

“Q. Did you have any settlement or adjustment with the Commissioner of Internal Revenue or his proper officers for the [72] *for the* year 1919, including the Bryson-Robison Corporation and your individual transactions on the subsequent years of 1920 and 1921?

“A. Yes, I had a report, acceptance of the accounts for those years.

“Q. I hand you an official offer of adjustment from the Commissioner's office, and I will ask you if you received that in due course of mail?

“A. Yes, I received it.”

(At this point the above document was offered and received in evidence and marked Exhibit No. 7).

I do not remember if I made up this offer but they evidently accepted it. I do not remember—for it was too far back—if there was an agreed form or a typed form of acceptance or rejection. I think that I received from the Government this \$7.45 that was found as a refund, but I do not know. I could

(Testimony of Elmer D. Bryson.)

trace that up evidently. I am forty-nine years old and I have been following the business and think that I am acquainted with the values of grazing or ranch lands in western Walla Walla County, Washington. I commenced as an owner of a sheep business in that portion of the county and state in 1909. Before that I had a six year experience there. I thought that I was familiar with the ordinary reasonable value of the lands which belonged to the Bryson-Robison Corporation, whether the same stood in the name of the corporation or in the names of the individual stockholders. I do not know exactly but the real estate worth that was conveyed to me by the deed from the Bryson-Robison Corporation and L. L. Robison and wife was around \$55,000 or \$60,000. We paid \$40,000 for part and bought more, but it really cost very nearly that. In connection with the conclusion reached by the Revenue Agent in Exhibit 7 wherein the value of this particular real estate covered by this conveyance was fixed [73] at \$53,000.00 and some odd, I think that it was the fair and reasonable market value of that land in 1919 at the time of this conveyance. I commenced the sheep business in 1903 and I have had practical experience in the range sheep business but not in thoroughbreds. That is in breeding, raising and growing of sheep. I had no other business and I attended to my duties as Secretary of the Bryson-Robison Corporation completely. I devoted practically all of my time to the corporate business; I had no other business and no other con-

(Testimony of Elmer D. Bryson.)

nections. I think the character of the services rendered by me were reasonably worth \$5,000 a year. Mr. Robison and myself were practically the sole and entire owners of the business and he and I agreed between ourselves that salary to each of us was proper. At the time I bought out the corporation from Mr. Robison there were obligations of the corporation which I later on liquidated in addition to the \$70,000. Roughly—for my memory is poor—I know there were notes at the bank and they had some store bills and we had accounts that had to be settled. I could not give them—only roughly. I am not sure but I think I owed the bank \$17,000 or \$18,000. I had a current merchandise account and some of the herders' wages were due. The 1919 wool clip was stored in Boston. We each took one-half. There were two cars. We shipped one in Mr. Robison's name and one in mine. When the proceeds came Mr. Robison turned over his profits to me and this money was used to pay off the debts. I would say as to a reasonable salary to Mr. Robison for the years he was connected with the corporation that he ought to have been equally allowed. The question did not come up when we were preparing the income tax return for the corporation. We treated our business as a private partnership, and there was no money in the business and when it was sold over, no money to take out. [74]

By Mr. Watson (counsel for respondent on review):

“Q. Mr. Bryson, I call your attention to the

(Testimony of Elmer D. Bryson.)

income tax return of the corporation for 1917, and particularly to deduction 4(b) of expenses in the sum of \$32,492.60, and ask you whether or not any compensation to yourself or Mr. Robison was included in that item?

* * * * *

“A. I do not remember all of the items that far back naturally, but I think there was \$5,000 for myself, I do not think there was in Mr. Robison’s case.”

Cross Examination.

I know, as a matter of fact, that all the expenses of the corporation were shown by checks that were drawn on the bank. I think you will find that there was \$5,000.00 paid to me for the 1917 return—that is, the 1917 return which was made in 1918. I believe the \$5,000 for 1917 was paid to me in 1918. I think I have those checks with me—I am not sure if I have them all or not. I have not signed a waiver of the tax liabilities involved in this proceeding in my own behalf. That is my signature on the waiver—Exhibit 5—of January 2, 1924. I did not remember it. I see now what that is. It is as former Secretary. I signed that, but then it is because it was requested. I did not sign that paper in my own behalf. I signed it on behalf of the Commissioner—he asked for a waiver, and that is what I gave him, or that is what was sent to the Bryson-Robison Corporation.

By Mr. McFarland:

“Q. Now, in this waiver it says, ‘In pursuance of the provisions of sub-division D, Section

(Testimony of Elmer D. Bryson.)

215 of the Revenue Act of 1921, the Bryson-Robison Corporation of Walla Walla, Washington, and the Commissioner of Internal Revenue hereby consent to a determination assessment and collection of the amount of income and excess profits tax and war profits tax due under any return made by or on behalf of said corporation for the years 1917, 1918 and so forth, signed by yourself, former Secretary of the Bryson-Robison Corporation, taxpayer. Now, you say that was not signed on behalf of the corporation and was not signed on your own behalf either?

“A. I signed it because it was requested.
[75]

“Q. I did not ask you why it was signed, but I asked you on whose behalf it was signed?

“Mr. WATSON: If your Honor please, the instrument speaks for itself.

“Mr. McFARLAND: No, I am simply asking the same question counsel asked in his direct examination.

* * * * *

By Mr. McFarland:

“Q. I will show you another waiver which counsel has heretofore examined, dated the 12th of February, 1923, and ask you if that signature Elmer D. Bryson, is your signature.

“A. Yes, that is my signature.”

(At this point there was offered and received in evidence the 1917 waiver of the Bryson-Robison

(Testimony of Elmer D. Bryson.)

Corporation, which document was marked Exhibit "E" and made a part of the record.)

"Mr. McFARLAND: Now if your Honor please, for the purpose of the record * * * I would like to read a part of that into the record:

"The MEMBER: Very well.

"February 12, 1923.

"Income and profits tax waiver.

"In pursuance of the provisions of subparagraph (d) Section 250, Revenue Act of 1921, Elmer D. Bryson of Walla Walla, Washington, and the Commissioner of Internal Revenue hereby consent to a determination, assessment and collection of the amount of any excess profits or war profits taxes due under any return made by or on behalf of said Bryson-Robison Corporation for the year 1917 under the Revenue Act of 1921, or any prior income or excess profits, war profits acts", and so forth.

"This waiver will be effective only one year from date of signing. Signed Elmer D. Bryson as former Secretary, Bryson-Robison Corporation, and signed D. H. Blair, Commissioner." There is a portion referring to certain statutes which I have omitted.

"Now, was that also given pursuant to a request from the Commissioner?

"A. It was; I did not remember it." [76]

That is my signature on the letter dated Walla Walla, Washington, February 7, 1924, addressed to

(Testimony of Elmer D. Bryson.)

the Commissioner of Internal Revenue, Washington, D. C., and signed Bryson-Robison Corporation by Elmer D. Bryson, formerly Secretary.

(At this point the above-described letter was offered and received in evidence, marked Exhibit "F" and made a part of this record).

"By Mr. McFARLAND: I offer in evidence the protest dated June 30, 1924, signed by Bryson-Robison Corporation, and Elmer D. Bryson, former Secretary * * * That is your signature, isn't it, Mr. Bryson?"

"A. Yes, sir, that is my signature."

(At this point the above-described document was offered and received in evidence, marked Exhibit "G" and made a part of the record).

I received the original of the copy of the letter dated January 27, 1924 addressed to Bryson-Robison Corporation, acknowledging receipt of my protest of January 2, 1924. I presume I received it, I do not know where the original is.

"By Mr. McFARLAND: Now, your Honor, * * * here is a claim for abatement which was dated the 5th of April, 1924, it says, * * * 'Deponent being duly sworn, according to law deposes and says that this statement is made on behalf of the above-named taxpayer.' Now the taxpayer's name is the Bryson-Robison Corporation, and it is signed Elmer D. Bryson, former Secretary, Bryson-Robison Corporation, Incorporated. I offer in evidence claim for

(Testimony of Elmer D. Bryson.)

abatement of taxes signed by this taxpayer at this time.”

(At this point the above-described document was offered and received in evidence, marked Exhibit “H” and made a part of the record.)

“Mr. McFARLAND: I offer another claim for abatement dated the 18th of April, 1924, the taxpayer named being the Bryson-Robison Corporation, Walla Walla, Washington, signed Elmer D. Bryson, former Secretary Bryson-Robison Corporation in which it states, ‘This deponent being duly sworn according to law deposes and says, this statement is made on behalf of the taxpayer named.’ ”

“Mr. BRYSON: I object to this being read in the record before the Exhibit is offered, or before we can offer an objection to it.”

“Mr. McFARLAND: I will withdraw that part that has been read.” [77]

(At this point the above-described document was offered and received in evidence, marked Exhibit “I” and made a part of the record.)

At the time of the transfer of the assets of the corporation, in June 1919 to me, Mr. Robison was President and I was Secretary of the corporation. In June, 1919, we had started dissolution proceedings. We really did not do much business as a corporation. I think we understood it more like a partnership. I bought out Mr. Robison. I just took possession of everything, that was all there

(Testimony of Elmer D. Bryson.)

was to it. It all occurred at the same time; we ceased to do business. After Mr. Robison got out of the corporation there was no corporation business done after I bought him out. After I bought him out, there was no change in officers at any time. We ceased to do business is all I can say, perhaps did not do it legally as a corporation should. That is my handwriting in Exhibit A—"Elmer C. Bryson, sole remaining officer"—but this is not (indicating). I do not know if that was in there when I signed it. I never saw that before. It is my signature, there is no question about that, but this is not my handwriting (indicating). That was signed February 24, 1920 and I presume that I signed that before Mr. Crowe. That other handwriting in the Schedule B is not my handwriting. "The officers wound up the property and turned back any property"—that is Mr. Crowe's handwriting, I guess. I think Mr. Crowe made out that return for me—he made most of our returns. I do not know what is meant by "sole remaining stockholder"—I did not put that on there—that is not my handwriting. I do not remember as to it, but it is my signature. It might have been written at that time, but I do not remember as to that. We have what books and records there are, but very little legal procedure is shown. I just took possession of the land and the property and that is all there was to it. There was no transfer further than that. [78]

"Q. Now, you took possession of every-

(Testimony of Elmer D. Bryson.)

thing at that time, transfer of the property and carried on the business?

“A. We were in charge of it prior. Of course, Mr. Robison was interested with me, naturally.”

“Q. Why didn't Mr. Robison answer some of his correspondence instead of you?

“A. Well, I made out all of the income tax returns and I did most of the business while we were together, and as far as that was, I was Secretary and Treasurer.”

“Q. Wasn't it because you felt that you were the sole person that was responsible, if anybody was responsible, for the affairs of the corporation?

“A. Well, I did settle all bills that were due the corporation. I took over everything and gave him \$70,000 for it.”

Redirect Examination.

(By Mr. Bryson, counsel for respondent on re-view):

The Robison corporate stock never was indorsed and delivered to me at all. We made an effort to locate the original stock book of the corporation; Mr. Crowe was unable to locate it, he said. Mr. Crowe had practically all of the corporate records when we ceased business in 1919, and he had all of those until quite recently. We were unable to locate the original stock book. I have my corporate stock somewhere among my papers here. After

(Testimony of Elmer D. Bryson.)

the transaction between myself and Mr. Robison in June, 1919, he ceased to have anything further to do with the corporation affairs. During the years we actively operated, I was manager in active charge with his consent and approval. The detailed work fell on my shoulders. I do not mean to say that he did not do any active work, but the management and secretary work, I took it. But insofar as looking after the property and helping to shear sheep and all of that, Mr. Robison helped, up until June 1919. Of course I did most of the book-keeping and most of the check paying as far as that was concerned, what little making out of checks there was. [79]

The witness was then excused.

LESTER L. ROBISON

one of the petitioners herein, having been previously sworn, was recalled and testified further as follows:

Direct Examination.

I have never seen Exhibit 5 before. I first learned of its existence about the time they were going to levy an individual assessment on my property. I do not know if this appeal had been begun or not at that time. I suppose Mr. Bryson had this correspondence with them, but I did not know anything about it until they were going to put an assessment or levy on my individual property. That is when I appealed to the Board. That was when I

(Testimony of Lester L. Robison.)

got a deficiency letter, in the fall of 1926 sometime. That was the first I knew of any such waiver as this ever having been made. I never at any time authorized Mr. Bryson or anyone else to make or execute any waiver. Right now is the first time I ever saw Exhibit E. I did not at any time authorize the execution of that waiver. I do not know when I first knew of its existence—unless it was either at the time they were going to assess this levy and I took it up with the Board of Tax Appeals or now. I never saw that until today.

“Q. Well, now, then, let us get clear. You say that you heard about that when, at the time you took your appeal?

“A. I heard that he had signed some kind of a waiver whether it is this waiver or not I do not know. He signed some kind of a waiver to the Government, but I do not know whether it was this one or which.

“Q. As far as these waivers are concerned you have not had anything to do with them or authorized them in any way?

“A. No, sir.”

I never at any time ever had any notice except the notice in that deficiency letter of November 23, 1926, of any assessment against the cor- [80] poration or against myself. I did not have anything to do with this correspondence. I was not consulted about the matter any. I did not have anything to do with those claims in abatement. I knew prac-

(Testimony of Lester L. Robison.)

tically nothing about the fact that there was anything in controversy, until I got that letter of assessment. During the time of the existence of the Bryson-Robison Corporation I was President of the corporation all of the time. There never was any change of officers in the corporation during the period of its existence, to my knowledge. I do not know of any time that the corporation authorized Elmer D. Bryson to execute any tax waiver as binding or otherwise on the corporation or any of its stockholders. As President of the corporation, had such been done I would have known of it.

By Mr. WATSON:

“Q. You have stated you were President of the corporation during its existence. Were you President of the corporation after you sold out to Mr. Bryson?

“A. I thought it was all over with and I just stepped out, never had anything more of it.”

Whereupon,

FRANK JOHNSON,

was called as a witness for and on behalf of the respondent on review, and after having been first duly sworn, was examined and testified as follows:

Direct Examination.

(By Mr. Watson:)

My name is Frank Johnson. I am Internal Rev-

(Testimony of Frank Johnson.)

enue Agent stationed at Walla Walla, and as such agent I made an examination of the income and profits tax liabilities of the Bryson-Robison Corporation for the years 1917, 1918 and 1919. I do not remember the date I made that examination, but it has been stated on the report. At the time of my examination I examined whatever books and records of the corporation there were. As shown by my examination of the books and records for the year 1917, there [81] were no salaries paid in 1917.

“Q. For the year 1917?

“A. None paid in 1919.”

If it is shown in my report that \$2500 for the year 1919 in the report made out in 1920 paid to Mr. Elmer D. Bryson, which constituted six months' salary at \$5,000 a year, that would be it. My testimony is entirely from memory without any immediate refreshing of my memory. My report shows that salaries were paid in 1918, and it was allowed simply as a matter of equity. My report shows that.

“Mr. McFARLAND: I think I will get your report so that we will have your memory refreshed, so that we won't have any guess work there.”

Cross Examination

That document right there is that report.

By Mr. McFarland:

“Q. Now, for the purpose of refreshing your

(Testimony of Frank Johnson.)

recollection, will you look at such portions of that report as may be necessary to refresh your recollection and state what salaries were paid during the years involved here, as shown by the books and records.

Mr. WATSON: If the Court, please, we admit that amount assessed. We claim the deduction for three years was disallowed. We do not claim that the salaries were actually in kind disbursed during 1918. In 1917 they had no income.

The MEMBER: It is admitted that there were no salaries actually paid in 1917, your contention being they incurred liability and to that extent did not pay it because they made no sales.

Mr. BRYSON: Not in that identical form.

Mr. McFARLAND: Does counsel contend they were ever paid?

Mr. BRYSON: That they were ever paid?

Mr. McFARLAND: Paid, yes.

Mr. BRYSON: Yes, they were paid when Elmer D. Bryson bought the [82] assets of the corporation and there was due him \$2500. He did not take it out of one pocket and put it in another. It was paid.

The MEMBER: Well, I suppose it is admitted without the necessity of going any further with this witness, that no salary was actually paid in 1917 or 1919.

Mr. McFARLAND: Or 1919.

(Testimony of Frank Johnson.)

The MEMBER: In money, that is admitted, isn't it?"

The books do not show any accrual of salaries. They did not keep any formal books of account, as a matter of fact they did not have any books of account—just long sheets of paper. They had no formal books of account.

Whereupon,

LESTER L. ROBISON,

one of the petitioners herein, having been previously duly sworn, was recalled to the stand and further examined and testified as follows:

I am forty-six years old. I now own about 8,000 acres of land in Walla Walla County. I have been in the farming and stock business every since I have been a boy, but actually engaged myself since 1907. I am familiar with the land that was held in the individual names for the Bryson-Robison Corporation. I know the fair and reasonable value of this land in 1917 and I can explain it in my own way. We purchased that original land for \$40,000.00 which was very reasonable. I owned some land in that neighborhood before, we gave Mr. Bryson \$40,000 for it. I cannot say how many acres or how many sections there were. I could ask Mr. Bryson; he could tell us. Yes, 10,360 is right. We purchased some more land in 1918. Values went up. We purchased it the land the corporation owned during the year 1917 in

(Testimony of Lester L. Robison.)

1916 for right at \$4.00 an acre. I think it advanced in 1917 at least a dollar an acre, and in 1918 maybe \$2.00 an acre. There was commencing in 1918 and during the War, the last part of the War there land increased awful high and they were jumping right along in 1919, but still [83] that did not change it. So that in 1917 the corporation owned lands including this held by the individuals for it of the value of \$50,000.00. And in 1919 or 1918 it had increased easily another dollar. As to its worth in 1919, I think land no better than that land, in different localities in our county sold for as high as \$7 or \$8 an acre for grazing land. It was pretty hard to keep track of values at that time. We could have readily sold it for at least \$60,000 in 1919. I took a first mortgage on the real estate alone for \$70,000.00 for which you sold out, and I considered myself well secured. It was pretty hard to set values of land at that time because they were all jumping up pretty high. I mean by value what it would bring.

“The MEMBER: Was this land purchased by the corporation or by you gentlemen as individuals?

“The WITNESS: I think we purchased it as individuals but with the understanding it would be the corporation. The corporation was not formed at first.

“The MEMBER: I understood you to say you traded in into the corporation for capital stock?

(Testimony of Lester L. Robison.)

“The WITNESS: Yes.

* * * * *

“Mr. BRYSON: Perhaps I should explain that to your Honor as to what was done. I personally owned 10,000 acres that was sold to the individuals at the time and closed up the deal and the corporation was formed. The individuals gave me their check and the land was deeded to the corporation.

“The MEMBER: At what price?

“Mr. BRYSON: They paid me \$40,000 and there were other lands that went into the corporate property at that time. Elmer D. Bryson owned other lands there and there were other lands that went into it in addition to the 10,300 acres I sold them, and they paid me cash for the 10,000 acres. * * * That was in the fall of 1916.

“The MEMBER: What I was trying to get at was the allegation of \$45,000 worth of land was excluded from invested capital, and it is now admitted that land should have been included and it was to get testimony to show the value. [84]

“Mr. BRYSON: That was carried in these controversies at a value of \$45,000, because it was listed as that, and excluded as that.”

Witness excused.

The foregoing evidence, together with the Exhibits referred to, is all of the material evidence adduced at the hearing before the Board of Tax Appeals, and the same is approved by C. M. Charest, General Counsel, Bureau of Internal Revenue, as attorney for the Commissioner of Internal Revenue.

(Signed) C. M. CHAREST

General Counsel,

Bureau of Internal Revenue.

The foregoing evidence, together with the Exhibits referred to, is all of the material evidence adduced at the hearing before the Board of Tax Appeals, and the same is approved by the undersigned as attorney for respondent on review.

The foregoing is all of the material evidence adduced at the hearing, and in order that the same may be preserved and made a part of this record, this statement of evidence is duly approved and settled this 25th day of July, A. D., 1933.

(Sgd.) EUGENE BLACK

Member,

United States Board of Tax Appeals.

[Endorsed]: United States Board of Tax Appeals.
Lodged Jun. 20, 1933.

[Endorsed]: United States Board of Tax Appeals.
Filed Jul. 25, 1933. [85]



SCHEDULE E.—CAPITAL, SURPLUS, AND
UNDIVIDED PROFITS AS SHOWN BY
BOOKS BEFORE ANY ADJUSTMENTS
ARE MADE THEREIN.

E4. Stock actually outstanding at the end of the preceding taxable period should be entered in this schedule to the extent that it is paid up. If stock or shares were issued at a nominal value or without par value the entries should reflect the amounts on the books in respect thereof at the close of the preceding taxable period.

E5. This item should include paid-in surplus per books at the end of the preceding taxable period. If any amount is claimed under Section 326 (a) (2) of the Revenue Act of 1918 or under Article 837 of Regulations 45, the amount claimed should be entered under Item 1, Schedule F, and not in this schedule.

E7. Reserves which represent allocations of surplus and were not accumulated through deductions made in computing net income as returned in previous years may, if properly explained, be entered on line 7. Such entries should be identified and if necessary reconciled with balance-sheet reserves.

E10. If the corporation had on hand at any time during the taxable period any treasury stock, copies of the journal entries covering the original issuance, repossession and any subsequent adjustments should be furnished. Treasury stock includes all stock reacquired by the corporation and not cancelled, regardless of the reason for the acquisition.

Item.	Amount.
Capital stock paid up and actually outstanding at the close of the preceding year:	
1. First preferred	\$.....
2. Second preferred
3. Common
4. Total	\$.....
Surplus and undivided profits:	
5. Paid-in surplus
6. Earned surplus and undivided profits
7. Reserves, additions to which are not deductible in computing net income (to be reconciled with balance-sheet items)
8. Other items (to be detailed)
9. Total of Items 4, 5, 6, 7, and 8	\$.....
10. Deduction on account of treasury stock
11. Capital and surplus at beginning of taxable period as shown by books	\$.....

**SCHEDULE F.—ADJUSTMENTS BY WAY OF
ADDITIONS.**

F1. If an addition to invested capital is claimed in Item 1, Schedule F, submit a statement showing (a) the kind of property, (b) the year in which it was paid in, (c) from whom acquired, explaining his relationship to the corporation, (d) the actual cash value of such property at the date when paid in, (e) the par value of stock or shares issued therefor and the amount at which such property was entered in the accounts, (f) the basis upon which the actual cash value of the property was determined and the date when such determination was made, and (g) the amount of depreciation sustained on such property from the date of acquisition to the beginning of the taxable period.

F2. If an addition to invested capital is claimed in Item 2, Schedule F, submit a statement showing (a) the kind of property, (b) the year in which it was acquired, (c) its cost, (d) the amount of depreciation sustained on such property from the date of acquisition to the beginning of the taxable period. State also whether each item sought to be restored was actually used or usable at the beginning of the taxable period. Were these expenditures, when made, written off in lieu of depreciation?..... If so, explain what adjustments have been made to provide for depreciation in view of the proposed restoration to surplus. Additions in this item are cumulative to the beginning of the taxable period. For all additions hereunder pro-

vision must be made for depreciation to the beginning of the taxable period.

F3. If any addition to invested capital is claimed in Item 3, Schedule F, state specifically the amount of depreciation written off each year in the books of the company and the amount allowed as a deduction in computing net income. Additions to this item are cumulative to the beginning of the taxable period.

Item.	Amount.
1. Actual cash value of tangible property clearly and substantially in excess of par value of stock issued therefor or of the cash or other consideration paid therefor (Articles 836 and 837)	\$
2. Additions to surplus (Articles 840 to 843)
3. Depreciation or depletion charged in accounts of the corporation but disallowed by the Department as a deduction on income-tax returns
4.
5.
6.
7. Total	\$

SCHEDULE G.—ADJUSTMENTS BY WAY OF DEDUCTIONS.

G1. Is any patent, copyright, secret process, or formula, good will, trade-mark, trade brand, franchise, or other similar intangible property, paid in for stock, carried as an asset by the corporation? If not entered specifically as such, is the intangible value merged under any other title or titles on the books or balance sheets submitted with this return? Is it entered on the books at a value in excess of its actual cash value when paid in? In excess of the par value of the stock issued therefor? Is the aggregate of such assets acquired prior to March 3, 1917, entered on the books at a value in excess of 25 per cent of the par value of the stock outstanding on March 3, 1917? Is the aggregate of such assets entered on the books at a value in excess of 25 per cent of the par value of the stock outstanding at the beginning of the taxable period?

If the answer to any of the foregoing questions is "yes," submit a statement showing separately with respect to such assets acquired (1) before March 3, 1917, and (2) on or after that date, (a) date of acquisition; (b) cash value at that date, with a complete explanation of the basis upon which such cash value was determined; (c) par value of the stock issued therefor; (d) par value of total stock outstanding March 3, 1917; (e) par value of total stock outstanding at the beginning of the tax-

able period; (f) the value at which such assets are entered on the books of the corporation.

If all the intangibles were acquired before March 3, 1917, the amount by which (f) exceeds (b), (c), 25 per cent of (d), or 25 per cent of (e), whichever is lowest, must be entered at Item 1, Schedule G, for the taxable period.

If the intangibles were acquired on or after March 3, 1917, the amount by which the entry in (f) relating to such intangibles exceeds (b) or (c) relating thereto, or 25 per cent of (e), whichever is lowest, must be included in Item 1, Schedule G, for the taxable period: Provided, That if intangibles were acquired before March 3, 1917, and also on or after that date, deduction shall be made so that the amount included in invested capital for the aggregate of intangibles shall not exceed 25 per cent of the par value of the total stock outstanding at the beginning of the taxable period.

Note—If the stock of the corporation was issued at a nominal value or without par value, for the purpose of the computation under Item 1, the par value shall be deemed to be the fair market value as of the date or dates of issue. The aggregate value so determined of stock outstanding on March 3, 1917, or at the beginning of the taxable period, shall be the basis for the computation.

G2. Is any tangible property, paid in for stock, carried as an asset by the corporation?
If so, is it entered on the books at a value in excess of its actual cash value when received?

In excess of the par value of the stock paid therefor?

If the answer to any of the foregoing questions is "yes" submit a statement showing (a) kind of property, (b) when acquired, (c) par value of the stock paid therefor, (d) actual cash value of the property when paid in, (e) the basis on which that value was determined, (f) value at which the property is entered on the corporation's books, and (g) amount by which such value exceeds the allowable value under Section 326 (a) (2) of the Revenue Act of 1918. Enter this amount as Item 2, Schedule G, for the taxable period.

G3. Was the business reincorporated, reorganized, or consolidated or was its ownership changed or was there a change in ownership of property after March 3, 1917? If so, answer the following questions:

(a) Did an interest of 50 per cent or more in the business or in the property which changed ownership remain in the control of the same persons, corporations, associations, or partnerships, or of any of them?

(b) Were any of the assets entered on the books of the corporation making this return at a higher value than on the books of its predecessor?

(c) If such previous owner was not a corporation, attach a statement showing (1) the cost of acquisition to the previous owner of any asset so transferred or received, (2) expenditures subsequent to that date for betterment or development not deducted as expense or otherwise since March

1, 1913, by such previous owner, (3) the allowance for depreciation, depletion, or impairment since the date of acquisition by such previous owner.

(d) If all, or substantially all, of the property was acquired from a corporation during the taxable period, attach hereto balance sheets of such predecessor corporation as at the beginning of the taxable period and as at the date immediately prior to the transfer of the property to the corporation making the return, and also a balance sheet or statement of the corporation making this return showing the values at which such property received or transferred were entered on the books.

For the purpose of determining invested capital each asset so transferred shall be valued (a) as if still in the possession of the previous owner, if a corporation, or, if not a corporation, (b) at its cost to such previous owner, with proper adjustments for losses and improvements.

G4. Is any property (including physical property, securities, and intangible property) paid for with cash or with other tangible property entered on the books of the corporation at a value in excess of the amount of cash paid therefor or the actual cash value of the tangible property paid therefor?

..... If so, submit a statement showing (a) kind of property, (b) amount of cash paid therefor, (c) actual cash value of other tangible property paid therefor, (d) how that value was determined, (e) value at which the property is entered on the books of the corporation, and (f) excess of

(e) over (b) or (c). This excess must be entered as Item 4, Schedule G, for the taxable period.

G5. Has adequate provision been made in the accounts of the company for (a) losses of every kind?, (b) depreciation?, (c) obsolescence?, (d) depletion of mineral deposits, timber supplies, and the like?

If adequate charge has not been made for depreciation, depletion obsolescence, and other losses, and the value of the property has not been maintained by replacements that have been charged to expense, proper additional charges therefor must be computed for all years in which they were not made on the books, and the total amount of such charges must be entered as Item 5, Schedule G.

Item.	Amount.
1. Valuation of patents, copyrights, secret processes, or formulae, good will, trade-marks, trade brands, franchises, or other intangible property	\$.....
2. Valuation of tangible property paid in for stock
3. Valuation of assets acquired in reorganizations
4. Appreciation
5. Depreciation, depletion, and other losses.....
6.
7.
8. Total Deductions	\$.....

SCHEDULE H.—CHANGES IN INVESTED CAPITAL DURING TAXABLE PERIOD.

1. Changes in invested capital during the taxable period ordinarily arise in one or more of the following ways:

Additions—

- (a) By sale of capital stock for cash or by the issue of capital stock for tangible or other assets.
- (b) By payment of assessments by stockholders or by creation of paid-in surplus by contribution of stockholders.

Deductions—

- (c) By liquidation of part of the capital by retirement of stock or by purchase of treasury stock not out of current earnings.
- (d) By payment of cash dividends out of earnings of prior years.
- (e) By payment of Federal income and profits taxes for the previous years.

The changes with respect to taxes will occur in nearly every case. Should no changes be noted, the reason for the omission should be stated.

2. The following instructions should be followed in making the above adjustments; each item should be designated as an addition or deduction, deduction being designated by red ink:

- (a) If stock is issued for cash, the actual cash received (but not the amount of discount) should be entered in this schedule. Assets (other than cash) paid in for stock must be valued in accord-

ance with Section 326 (a) (2) of the Revenue Act of 1918.

(c) If capital stock of the corporation is re-acquired but not paid for out of current profits, the cost of such stock should be deducted from invested capital.

(d) Report dividends paid out of profits of prior years but not dividends paid out of profits of the taxable period. Any distribution made during the first 60 days of the taxable period shall be deemed to have been made from earnings or profits accumulated during preceding taxable period; but any distribution made during the remainder of the taxable period shall be deemed to have been made from the profits for that period to the extent that such profits are sufficient. (See Article 1542.)

(e) The amount of Federal income and profits taxes payable should be prorated and deducted as of the dates when due and payable whether reserves have been set up on the books or not. (See Article 245.)

3. The data called for in columns 1 to 5 should be given for all transactions, except that columns 3 and 4 are applicable only to the issue or reacquisition of the corporation's stock.

4. In column 6 enter the number of days remaining in the taxable period (including the date of change).

5. The net changes not reported in Schedule L, if not in accordance with the increases or decreases reflected in the balance sheets, should be fully reconciled therewith.

1. Nature of additions and deductions.	2. Date.	3. Number of shares sold or reacquired.	4. If for cash, state price per share.	5. Amount of cash or cash value actually received or paid out.	6. Number of days effective.	7. Adjusted average. Column 5 x Column 6 No. days in taxable period.
1			\$	\$		
2						
3						
4						
5						
6						
7						
8						
9						

SCHEDULE J.—INADMISSIBLE ASSETS.

Has the corporation any inadmissible assets (i. e., stocks, bonds, and other obligations, except obligations of the United States, the income from which is not taxable)?

If so, attach hereto a statement showing for the taxable period the facts called for in items (a) to (j) of this schedule.

If the income from such assets consists in part of gain or profit from the sale or other disposition thereof, or if all or part of the interest derived from such assets is in effect included in the net income because of the limitation on the deduction of interest under Section 234 (a) (2) of the Revenue Act of 1918, then a corresponding part of the capital invested in such assets is deemed an admissible asset. In such case set forth in detail—

- (a) the various kinds of income derived from such assets and the computation of the part of the capital invested therein which is deemed an admissible asset.

For the purpose of this schedule inadmissible assets shall be valued at cost of acquisition, except that if the taxpayer is a dealer in securities and inventories such assets in accordance with Article 1585, Regulations 45, such inventory figure shall constitute the measure of value. Admissible assets shall be valued as provided in Sections 326, 330, and 331 of the Revenue Act of 1918 and Articles 831-869, 931-934, and 941 of Regulations 45. The average amount of assets of each kind held during

any year may ordinarily be determined by dividing by 2 the sum of the amount of such assets held at the beginning of the taxable period and the amount held at the end of the taxable period. In such case the amount of admissible assets may best be determined from (1) the balance sheet as at the beginning of the period adjusted with respect to the items in Schedules F and G and (2) the balance sheet as at the end of the period correspondingly adjusted. But if at any time during the taxable period a substantial change has taken place in the amount of such assets, the average amount must be determined as provided in Article 852 of Regulations 45. In such case show in detail—

- (b) The computation of such amount;
- (c) Amount of inadmissible assets held at beginning of the taxable period;
- (d) Amount of inadmissible assets held at end of taxable period;
- (e) Average amount of inadmissible assets held during taxable period;
- (f) Amount of admissible assets held at beginning of taxable period;
- (g) Amount of admissible assets held at the end of taxable period;
- (h) Average amount of admissible assets held during taxable period;
- (i) Sum of (e) plus (h);
- (j) Percentage which (e) is of (i).

This percentage (j) should be applied to the amount appearing on line 7, Schedule B, in order

to obtain the deduction on account of inadmissible assets, which should be entered on line 8, Schedule B. [87]

QUESTIONS.

KIND OF BUSINESS.

1. By means of the key letters given below, identify the corporation's main income-producing activity with one of the general classes, and follow this by a special description of the business sufficient to give the information called for under each general class.

(A) Agriculture and related industries, including fishing, logging, ice harvesting, etc., including the leasing of such property. State the product or products. (B) Mining and quarrying, including gas and oil wells. Include the leasing of such property. State the product or products. (C) Manufacturing. State the product and also the material if not implied by the name of the product. (D) Construction. Excavations, buildings, bridges, railroads, ships, etc., also equipping and installing same with systems, devices, or machinery, without their manufacture. State nature of structures built, materials used, or kind of installations. (E1) Transportation—rail, water, local, etc. State the kind and special product transported, if any. (E2) Public utilities, gas, natural, coal, or water; electric light or power, hydro or steam generated; heating, steam or hot water; telephone; waterworks or power. (E3) Storage without trading or profit from sales. Elevator, warehouses, stockyards, etc. State pro-

duct stored. (E4) Leasing transportation or utilities. State kind of property. (F) Trading in goods bought and not produced by the trading concern. State manner of trade, whether wholesale, retail, or commission, the product handled. Sales with storage with profit primarily for sales. (G) Service, domestic, including hotels, restaurants, etc.; amusements; other professional personal, or technical service. State the service. (H) Finance, including banking, real estate, insurance. (I) Concerns not falling in above classes (a) because of combining several of them with no predominant business, or (b) for other reasons.

2. Concerns whose business involves activity falling in two or more of the above general classes, where the same product is concerned, should report business as identified with but one of the above general classes; for example, concerns in A or B which also transport and market their own product exclusively or mainly, should still be identified with classes A or B; concerns in C (manufacturing) which own or control their source of material supply in A or B and which also transport, sell, or install their own product exclusively or mainly, should be identified with manufacturing; concerns in D may control or own source of supply of materials used exclusively or mainly in their constructive work; concerns in E1 or E2 may own or control the source of their material or power; concerns in F may transport or store their own merchandise, but its production would identify them with A, B, or C.

3. Answers:

- (a) General class (use key-letter designation).....
- (b) Main income-producing business (give specifically the information called for under each key letter, also whether acting as principal, or as agent on commission; state if inactive or in liquidation)
-
-
-

OTHER CONCERNS IN SAME BUSINESS.

4. Enter on the following lines the names and addresses of five representative concerns in your locality or section of the country engaged in the same kind of business:

.....

.....

.....

.....

.....

INCORPORATION.

5. Date of incorporation
6. Under the laws of what State or country?.....
-

REORGANIZATION AND ACQUISITION OF MIXED AGGREGATES OF ASSETS.

7. Has the corporation, or any of its predecessors, been reorganized, or has it, or a predecessor, taken over a going business or acquired a mixed

aggregate of tangible property, patents, and copyrights, and good will and other similar intangible property, and paid for such property in whole or in part with stock or other securities since the close of the preceding taxable period?

8. If so, furnish a brief narrative history of the business and submit a statement showing:

(a) The name of the concern taken over (or from which the property was acquired);

(b) The nature of the assets and liabilities so acquired;

(c) The total par value of the stock issued therefor;

(d) The value at which each class of assets was carried on the books of the concern from which acquired (submit a balance sheet of the predecessor concern as at the date of acquisition or as at the close of its last accounting period prior thereto);

(e) The value at which each item was entered in the books of the corporation making this return, and full details of any adjustments subsequently made pertaining thereto and the basis on which such revaluation was made.

9. If patents, copyrights, secret processes or formulæ, good will, trade-marks, trade brands, franchises, or other intangible property were acquired, state also the basis on which their value was determined and how they were paid for.

10. If at the time of any purchase or reorganization as contemplated in question 7, any property was entered on the books of the reorganized concern

or any vendee predecessor at a value in excess of that at which it was carried on the books of the vendor concern, state the basis on which the re-valuation was made.

AFFILIATIONS WITH OTHER CORPORATIONS (TO BE ANSWERED BY EVERY CORPORATION).

11. Do you own directly or control through closely affiliated interests or by a nominee or nominees over 50 per cent of the outstanding voting capital stock of another corporation or of other corporations?

12. Is over 50 per cent of your outstanding voting capital stock owned by another corporation or by two or more corporations that are affiliated?.....

13. Is over 50 per cent of your outstanding voting capital stock as well as over 50 per cent of the outstanding voting capital stock of another corporation or of other corporations owned or controlled by the same individual or partnership or by the same individuals or partnerships?

14. If the answer to questions 11, 12, or 13, or any of them is "yes," procure from the Collector of Internal Revenue for your district Affiliated Corporations Questionnaire, Form 819, which shall be filled out and filed as a part of this return.

VALUATION OF CAPITAL STOCK.

15. What was the fair value of the total capital stock of the corporation as determined in the last assessment, if any, of the capital stock tax \$.....
Date of that assessment?

PREDECESSOR BUSINESS.

16. Did you file a return under the same name for the preceding taxable period? Answer "Yes" or "No" If not, was your corporation in anyway an outgrowth, result, continuation, or re-organization of a business or businesses which was in existence during the taxable or preceding period? Answer "Yes" or "No" If answer is "yes," give name and address of each predecessor business.

.....

.....

BASIS OF RETURN.

17. Is this return made on the basis of actual receipts and disbursements?
If not, describe fully what other basis or method was used in computing net income

GOVERNMENT CONTRACTS.

18. Have any adjustments been made during the taxable period on account of contract or contracts between the Government or its agencies or in any Government contract or contracts in which you derived income directly or indirectly, through the operations of a claim board or otherwise? Answer "Yes" or "No." If so, state the amounts involved \$.....; whether or not such amounts are included in this return.....; and, if not, was an amended return for 1918, accounting for the additional income, filed?
Submit a schedule showing full particulars of the contract, date entered into, date the work ceased

under said contract or contracts, and the amount and nature of the adjustment.

PREPARATION OF RETURNS.

19. Did you employ anyone especially to prepare or advise in the preparation of this return? Answer "Yes" or "No" If so, give name and address

LIST OF ATTACHED SCHEDULES.

Enter below a list of all schedules accompanying this return, giving for each a brief title and the schedule number.

.....

.....

.....

None—Business closed.

SCHEDULE K.—BALANCE SHEETS.

Attach hereto balance sheets as of the beginning and end of the taxable period (preferably in parallel columns), showing as nearly as practicable the details called for below. (These balance sheets should be prepared from the books and should be in agreement therewith, or any differences should be reconciled, and if this is a consolidated return, balance sheets should be furnished in accordance with paragraph 7 of page 1 of Instructions.)

ASSETS.

Cash (including cash in bank, and on hand, certificates of deposit, etc.).

Trade accounts (before deducting reserves for losses).

Notes receivable from customers.

Other accounts and notes receivable (to be classified).

Inventories:

Raw Materials.

Work in progress.

Finished products.

Supplies.

Investments:

Bonds—

U. S. bonds and obligations (each issue to be stated separately).

Exempt (municipal, State, etc.).

Other.

Stock of corporations—

Foreign.

Domestic.

Loans and advances:

To officers and employees.

To others.

Deferred charges to future operations (to be detailed).

Fixed assets:

Land.

Buildings.

Machinery.

Tools and minor equipment.

Delivery equipment.

Office furniture.

Other (state character).

Total.

Less reserves for depreciation (show separately amount applicable to each fixed asset).*

Net Value.

Patents, good will, and other intangible assets:

 Paid for in cash or other tangible property.

 Paid for in stock (other than stock dividends).

 Created by stock dividends or otherwise.

Discount:

 On bonds.

 On stock.

 Total.

LIABILITIES.

Notes payable:

 To officers and stockholders.

 To others (including bank loans).

Accounts payable:

 Trade.

 Other.

Accrued expenses and reserves, the charges creating which are allowable deductions from income (to be detailed).

Reserves, the charges creating which are not allowable deductions from income:

 Reserves for losses on notes and accounts receivable.

 Other reserves (to be detailed).

Capital stock outstanding (to be classified).

Surplus and undivided profits.

 Total.

*Reserves for depreciation may be deducted from the respective asset account or itemized on the liability side of the balance sheet.

All corporations engaged in an interstate and intrastate trade or business and reporting to the Interstate Commerce Commission and to any national, State, municipal, or other public officer, may submit in lieu of above Form copies of their balance sheets prescribed by said Commission or State and municipal authorities, as at the beginning and end of the taxable period.

SCHEDULE L.—ANALYSIS OF SURPLUS ACCOUNT.

Attach hereto an analysis of the corporation's surplus account, showing the details of all adjustments of surplus for the taxable period, as nearly as practicable in the following form:

1. Surplus at beginning of taxable period as shown by books.

Add: 2. Total net profit as shown by books (Item 1, Schedule M).

3. Other credits to surplus (to be detailed).

4. Total of Items 1, 2, and 3.

Deduct: 5. Dividends (state date declared and date and amount of each payment, also whether in cash or in stock, and out of which year's earnings paid).

6. Other debits to surplus (to be detailed).

7. Total of Items 5 and 6.

8. Surplus at end of year as shown by books.

If this is a consolidated return, analyses should be furnished in accordance with paragraph 7, page 1, of Instructions. [88]

SCHEDULE M.—RECONCILIATION OF NET PROFIT AS SHOWN BY BOOKS WITH TAXABLE NET INCOME.

1. Net profit for taxable period as shown by books, before any adjustments are made therein	\$
2. Unallowable deductions:	
(a) Donations, gratuities, and contributions	
(b) Income, war-profits, and excess-profits taxes paid or accrued to the United States, its possessions, or a foreign country	
(c) Special improvement taxes tending to increase the value of the property assessed	
(d) Furniture and fixtures, additions, or betterments treated as expenses on the books	
(e) Replacements covered by depreciation	
(f) Insurance premiums paid on the life of any officer or employee for the benefit of the corporation or business	
(g) Interest on indebtedness incurred or continued to purchase or carry obligations or securities (other than obligations of the United States issued after September 24, 1917), the interest upon which is wholly exempt from taxation	
(h) Additions to reserves for bad debts, contingencies, etc. (to be detailed)	
(i)	

- (j)
 (k)
 (l)
 (m) Other unallowable deductions (to be detailed)
 (n)
3. Distributive share of net income, earned during period by personal service corporations not received or accrued on books.....
 4. Amount necessary to adjust book profit or loss with the amounts reported in Items 22 and 23, Schedule A (unless entry belongs on line 8).....
 Total \$.....
5. Nontaxable income:
 (a) Interest on obligations of the United States and its possessions, wholly exempt \$.....
 (b) Interest on obligations of States, Territories, and political subdivisions thereof
 (c) Interest on Farm Loan Bonds issued under Federal Farm Loan Act.....
 (d) Dividends on stock of domestic corporations and from foreign corporations taxable by United States upon any portion of their net incomes.....
 (e) Dividends on stock of personal service corporations out of earnings upon which a Federal income tax has been imposed
 (f) Other items of nontaxable income (to be detailed)
 (g)

(h)	.....	.....
(i)	.....	.....
7. Charges against reserves for bad debts, contingencies, etc. (to be detailed)	.....	.....
(a)	.....	.....
(b)	.....	.....
(c)	.....	.....
(d)	.....	.....
8. Amount necessary to adjust book profit or loss with the amounts reported in Items 22 and 23, Schedule A (unless entry belongs on line 4)	.....	.....
9. Taxable net income (Item 27, Schedule A)	.....	.....
10. Total	.....	\$ .....

SUPPORTING SCHEDULES.

The following schedules must be filled out in support of Schedule A, page 1, and firmly attached to this Return:

SCHEDULE A2: COST OF GOODS SOLD, EXCLUSIVE OF EXPENSES, REPAIRS AND OTHER ITEMS CALLED FOR SEPARATELY. (Secure from the Collector of Internal Revenue and file as a part of this Schedule Certificate of Inventory, Form 1126.)

Merchandise bought for sale.....	\$.....
Cost of manufacturing or otherwise producing goods. (Submit schedule showing principal items of cost.).....	.....
Plus inventories at beginning of year .....	.....
Total	\$.....
Less inventories at end of year.....	.....
Cost of goods sold .....	.....

NOTE.—Inventories must be valued at (a) cost or (b) cost or market, whichever is lower, provided that whichever basis is used must be applied to each item in the inventory and not to a part only. Inventories at the end of the taxable period must be value on the same basis as those at the end of the preceding taxable period, unless permission to make a change has been first obtained from the Commissioner.

If claims for losses on inventories or rebates on sales made under Section 214 (a) 12 of the Revenue Act of 1918 have been allowed, the opening invent-

ory must be correspondingly adjusted (see Article 266 of Regulations [illegible])

State here which of the above-mentioned bases for valuing inventories is used in this return.....

SCHEDULE A3: GROSS INCOME FROM OPERATIONS OTHER THAN TRADING OR MANUFACTURING.

Submit a schedule showing the nature and amount of the principal items included. See Schedule A, Item 3. (For insurance companies see paragraphs 2 and 3, page 2, General instructions.)

SCHEDULE A4: INTEREST ON OBLIGATIONS OF UNITED STATES OR ITS POSSESSIONS NOT EXEMPT.

Enter in table below the maximum amount of Liberty Bonds and other obligations of the United States issued since September 1, 1917 (par value), held at any one time, and War Finance Corporation Bonds from which interest was derived during the taxable period.

1. Class of Obligation.	2. Maximum Amount of Obligations.	3. Maximum Exemption.
(a) First Liberty Loan converted into Second Loan and Second Liberty Loan unconverted	\$.....	\$45,000 (See Note A.)
(b) First and Second Liberty Loans con- verted into Third Loan and Third Liberty Loan	\$20,000 (See Note B.)
(c) First Liberty Loan converted into Fourth Loan	\$30,000
(d) Fourth Liberty Loan	\$30,000
(e) Other United States obligations, ex- cept class (f), issued since Septem- ber 1, 1917	
(f) Victory Liberty Loan 4¾% Notes	None.
(g) War Finance Corporation Bonds	\$5,000 (See note C.)

Note A.—This exemption (maximum \$45,000) is limited to one and one-half times the amount of bonds of the Fourth Liberty Loan originally subscribed for and still held. State here amount of bonds of the Fourth Liberty Loan originally subscribed for and still held: \$.....

Note B.—This exemption (maximum \$20,000) is limited to three times the amount of notes of the Victory Liberty Loan originally subscribed for and still held. State here amount of notes of the Victory Liberty Loan, $3\frac{3}{4}\%$ and $4\frac{3}{4}\%$, originally subscribed for and still held. \$.....

Note C.—This exemption is separate from the \$5,000 exemption allowed on other obligations and can only be claimed against War Finance Corporation bonds.

Interest upon First Liberty Loan $3\frac{1}{2}\%$ and Victory Liberty Loan $3\frac{3}{4}\%$ convertible gold notes is exempt from all income and profits taxes. Interest upon all other issues of Liberty Loan Bonds as well as interest upon certificates of indebtedness and War Saving certificates is exempt from normal income tax regardless of the amount of the principal and is exempt from profits taxes, only to the extent provided for in the act authorizing the issue and subsequent acts. If your holdings are in excess of the exemptions specified above, secure Form 1125 from Collector and compute taxable interest. Interest on War Finance Corporation bonds is exempt from all normal income tax and is exempt from profits taxes only with respect

to a principal not exceeding \$5,000. This exemption is in addition to the exemptions above referred to.

SCHEDULE A5: INTEREST FROM OTHER SOURCES.

Submit a schedule showing the source, nature, and amount of the principal items included herein, the minor items being grouped in one figure. The total of the schedule should be entered as Item 5, Schedule A.

(1) Have you included in this item any interest on preferred stock? If so, how much? \$.....

(2) Have you included in this item any Federal income tax paid at source in pursuance of tax-free covenant bonds? If so, how much? \$.....

For interest on foreign bonds submit a schedule showing (a) name of country, (b) kind of obligations (whether national, State, municipal, or corporate obligations), (c) amount of principal, and (d) amount of interest.

SCHEDULE A6: INCOME FROM RENTALS.

Rentals to be reported as income will include all accruals as rent on buildings or other property owned or controlled by the corporation making the return. (Schedule A, Item 6.)

SCHEDULE A9: DIVIDENDS ON STOCK OF FOREIGN CORPORATIONS.

Submit a schedule showing (1) with respect to foreign corporations taxable by the United States

upon any portion of its net income, (a) name of corporation, (b) country in which organized, (c) total par value of stock held, and (d) amount of dividends; (2) same information with respect to foreign corporations not taxable by the United States upon any portion of the net income.

**SCHEDULE A10: GROSS INCOME FROM ALL
OTHER SOURCES EXCEPT DIVIDENDS**
(not including any amount in respect to sale of capital assets or miscellaneous investments).

Submit a schedule showing the source, nature, and amount of the principal items included herein, the minor items being grouped in one figure. The total of the Schedule should be entered as Item 10, Schedule A.

**SCHEDULE A12: ORDINARY AND NECES-
SARY EXPENSES** (except amounts called for separately in Schedule A and not including cost or value of capital assets or miscellaneous investments sold during taxable period).

Submit a statement showing character and amount of the principal items included in Item 12, Schedule A. (For schedules to be submitted by insurance companies see paragraphs 4 to 7, page 2, General Instructions.)

**SCHEDULE A13: COMPENSATION OF
OFFICERS.**

Submit a schedule showing for each officer (1) name, (2) duties, (3) time devoted to such duties, (4) shares of stock owned or controlled; (a) pre-

ferred, (b) common; (5) total compensation for the taxable period, and (6) amount of, and reason for increase, if any, over preceding period.

Submit a schedule showing for each employee (if a stockholder of the corporation), whose compensation is at the rate of \$3,000 or more per annum, facts similar to those called for in respect to officers.

SCHEDULE A14: REPAIRS (including labor, supplies, overhead, and other items properly chargeable to repairs).

Submit a schedule showing the nature and amount of the principal items included in Item 14, Schedule A. (For classification of repairs see paragraph 8, page 2, General Instructions.)

SCHEDULE A17: DEBTS ASCERTAINED TO BE WORTHLESS AND CHARGED OFF WITHIN TAXABLE PERIOD.

Submit a schedule showing the amount (a) arising from sales, or services previously reported as income; (b) arising from other sources (interest, rent, royalties, etc.) previously reported as income; (c) arising from sources other than those specified above (to be itemized).

SCHEDULE A18: EXHAUSTION, WEAR AND TEAR (INCLUDING OBSOLESCENCE).

If a deduction is made on account of depreciation, the following schedule must be filled in, and the total amount claimed in this schedule should correspond with the figures reflected in the balance sheet. (See General Instructions, page 2.)

Kind of property (If buildings, state the material of which con- structed.)	Date acquired	Cost or fair market value as at March 1, 1913, if acquired prior thereto.	Probable life after acquisition.	Amount of depreciation charged off.	
				This year.	Previous years.
		\$	\$	\$	\$
Total		\$	\$	\$	\$

Note.—If obsolescence is a factor in determining your deduction attach a statement showing the amount claimed for the taxable period and the basis on which computed.

**SCHEDULES A22 and A23: PROFIT OR LOSS
ON SALES OF CAPITAL ASSETS** (including liquidating dividends and miscellaneous investments, and losses sustained during the taxable period from fire, storm, or other casualty, or from theft, not compensated for by insurance or otherwise).

In case of sale of capital assets during taxable period, report the following information:

- (1) Original cost of assets \$.....
 - (a) Date of acquisition
 - (b) Kind of asset
- (2) Fair market price or value as of
March 1, 1913, if acquired prior
thereto
- (3) Cost of subsequent improve-
ments, if any
- (4) Depreciation, depletion, obsol-
escence, or amortization to date
of sale:
 - (a) Shown by books \$.....
 - (b) Accrued but not
on books \$.....
- (5) Net cost (Item 1 or Item 2,
plus Item 3, minus Item 4).....
- (6) Price at which assets were sold
or amount of liquidating div-
idends received

(7) Profit or loss

(a) If loss, report amount of
salvage, insurance, or
other recovery, if any \$.....

(b) Date loss charged off.....

State also how and by whom fair
market price or value as of March
1, 1913, was determined.....

Report what amount, if any, of the
value above includes good will..... \$.....

In case of exchange of investments submit evidence substantiating the basis used by you in arriving at the cash value of property received in exchange for other property.

SCHEDULE A26: AMORTIZATION OF WAR FACILITIES.

The amount claimed as a deduction under this item should be substantiated by schedule prepared in accordance with Section 214 (a) 9, Revenue Act of 1918, Articles 181 to 188, inclusive, of Regulations 45, and Treasury Decision 2859, amending Article 184. The specific information to be submitted is outlined in Article 188, Regulations 45.

DISCOUNT AND PREMIUM ON BONDS SOLD.

There must be attached to the return a schedule showing in detail each issue and sale of bonds of the reporting corporation giving the following information: (a) Class; (b) date of sale; (c) maturity; (d) amount sold; (e) amount realized; (f) premium or discount per annum.

That proportion of the premium or discount applicable to the return period must be reported either as Item 10 or 15, Schedule A, page 1, unless the amount of premiums or discount has been reported as income or allowed as a deduction in prior years. (See Article 544, Regulations 45).

We, the undersigned, president and treasurer of the corporation, for which this return is made, being severally duly sworn, each for himself deposes and says that this return, including the accompanying schedules and statements, has been examined by him and is, to the best of his knowledge and belief, a true and complete return made in good faith pursuant to the Revenue Act of 1918 and the Regulations issued thereunder.

[Seal of officer making affidavit.]

ELMER D. BRYSON

Treasurer.

Sole remaining officer.

Sworn to and subscribed before me this 24th day of February, 1920.

W. F. CROWE

Notary Public

(Official capacity.) [89]

[Endorsed]: U. S. Board of Tax Appeals, Div. 15, Docket 22184. Admitted in Evidence Jun. 2, 1930. Respondent's Exhibit B.

[Insignia]

United States of America
TREASURY DEPARTMENT
Washington

May 21, 1930.

PURSUANT to the provisions of Section 661, Chapter 17, Title 28 of the United States Code (Section 882 of the Revised Statutes of the United States), I hereby certify that the annexed are true copies of Assessment Certificate and that portion of the March, 1924, Special #17, income tax assessment list—Washington collection district—showing an additional assessment of \$5,896.86 for [illegible] against Bryson-Robinson Corporation, c/o Elmer D. Bryson, Walla Walla, Washington, on file in this Department.

IN WITNESS WHEREOF, I have hereunto set my hand, and caused the seal of the Treasury Department to be affixed, on the day and year first above written.

By direction of the Secretary of the Treasury:

[Seal]

F. A. BIRGFELD,
Chief Clerk, Treasury Department. [90]

Treasury Department, Internal Revenue Service. March, 1922.					Page No. 0	
ASSESSMENT LIST. SPECIAL 17						
District WASHINGTON, INCOME TAX MARCH 1924, # LIST						
(Classification.)						
	Old Balance	Date	Debit	Credit	New Balance	Remarks
0						
1						
2						
3						
4	BRYSON-ROBINSON CORP.				5896.86	1917 45502283
	C/o ELMER D BRYSON					NC 250 D
	WALLA WALLA WASH					OA 12/4/23
	MAR 04 SPL 17					
5						
6						
7						
8						
9						

[92]

[Endorsed]: U. S. Board of Tax Appeals, Div. 15, Docket 22184. Admitted in evidence Jun. 2, 1930. Respondent's Exhibit C.

[Insignia]

United States of America
TREASURY DEPARTMENT
Washington

May 21, 1930.

PURSUANT to the provisions of Section 661, Chapter 17, Title 28 of the United States Code (Section 882 of the Revised Statutes of the United States), I hereby certify that the annexed are true copies of Assessment Certificate and that portion of the September 1925, Special No. 1, income tax assessment list—Washington collection district—showing an additional assessment of \$5,[illegible] for 1918, against Bryson-Robison Corporation, Inc., Walla Walla, Washington, on file in this Department.

IN WITNESS WHEREOF, I have hereunto set my hand, and caused the seal of the Treasury Department to be affixed, on the day and year first above written.

By direction of the Secretary of the Treasury:

[Seal]

F. A. BIRGFELD

Chief Clerk, Treasury Department. [93]

Treasury Department
Internal Revenue Service
Form 23C-1—Revised April, 1925
Assessment Certificate

COMMISSIONER'S ASSESSMENT LIST
District of Washington
Month September Spl No. 1
Year 1925

Additional Assessments made by Commissioner:

Personal	\$.....
Corporation	\$ 5,741.89

.....
.....
.....
.....
.....

Total Assessments \$ 5,741.89

I hereby certify that I have made inquiries, determinations, and assessments of taxes, penalties, etc., of the above classification specified in these lists, and find that the amounts of taxes, penalties, etc., stated as corrected and as specified in the supplementary pages of this list made by me are due from the individuals, firms, and corporations opposite whose names such amounts are placed, and that the amount chargeable to the collector is as above.

D. H. BLAIR

Commissioner of Internal Revenue. [94]

Dated at Washington, D. C.
Office of Commissioner of Internal Revenue,
Sep. 1, 1925.

Treasury Department,
Internal Revenue Office.
..... March, 1922.

Page No.

ASSESSMENT LIST.

District Washington, Income Tax, List September 1925 Special No. 1

(Classification.)

Old Balance	Date	Debit	Credit	New Balance	Remarks
				5741.89	SEC 274 D RAR
				1918	438626
				OL	8/17/25

SEPT 00 C SPL NO 1

Information indicates this taxpayer is in process of dissolution. Verify.
If information is correct, notify proper parties of personal liability under
Revised Statutes Sections 3466 and 3467 if other creditors are paid be-
fore this tax is satisfied.

Elmer D. Bryson

5741.89

[95]

[Endorsed]: U. S. Board of Tax Appeals, Div. 15,
Docket 22184. Admitted in evidence Jun 2, 1930.
Respondent's Exhibit D.

[Insignia]

United States of America
TREASURY DEPARTMENT
Washington

May 21, 1930.

PURSUANT to the provisions of Section 661, Chapter 17, Title 28 of the United States Code (Section 882 of the Revised Statutes of the United States), I hereby certify that the annexed are true copies of Assessment Certificate and that portion of the March 1925, Special #7, income tax assessment list—Washington collection district—showing an additional assessment of \$2,973.54 for [illegible] against Bryson Robinson Corporation, Walla Walla, Washington, on file in this Department.

IN WITNESS WHEREOF, I have hereunto set my hand, and caused the seal of the Treasury Department to be affixed, on the day and year first above written.

By direction of the Secretary of the Treasury:

[Seal]

F. A. BIRGFELD,
Chief Clerk, Treasury Department. [96]

Treasury Department
Internal Revenue Service
Form 23C-1—Mar., 1923.

Assessment Certificate
COMMISSIONER'S ASSESSMENT LIST
District of Washington
Month March Special #7
Year 1925

Additional Assessments made by Commissioner:

Personals	136,336.01
Corporations	50,878.17

.....
.....
.....
.....

Total Assessments \$187,214.18

I hereby certify that I have made inquiries, determinations, and assessments of taxes, penalties, etc., of the above classification specified in these lists, and find that the amounts of taxes, penalties, etc., stated as corrected and as specified in the supplementary pages of this list made by me are due from the individuals, firms, and corporations opposite whose names such amounts are placed, and that the amount chargeable to the collector is as above.

C. R. NASH

Acting Commissioner of Internal Revenue. [97]
Dated at Washington, D. C.
Office of Commissioner of Internal Revenue,
Mar. 14, 1925.

Treasury Department, A S
Internal Revenue Service.
..... March, 1922.

Page No. 0

ASSESSMENT LIST

District Washington, Income Tax, List Corporation Spl #7
(Classification)
March 1925

Old Balance	Date	Debit	Credit	New Balance	Remarks
-------------	------	-------	--------	-------------	---------

0
1
2
3
4
5
6
7
8

BRYSON ROBINSON CORP
WALLA WALLA WASH

2973.54	1919 402204	9
	SEC 274 D	
	OA	
	OL 3/14/25	

MAR 09 C SPL # 7

[98]

[Endorsed]: U. S. Board of Tax Appeals, Div. 15, Docket 22184. Admitted in evidence Jun. 2, 1930. Respondent's Exhibit E.

Internal Revenue Agent

Feb. 15, 1923

Rec'd Seattle Division

It:Ca:Ms.

2506 = W.H.S.

Attach to 1917 return

45 = 502-283

Unaudited. Return. See + Please file.

Seattle, Wash.

Feb. 12, 1923

(Date)

INCOME AND PROFITS TAX WAIVER

In pursuance of the provisions of subdivision (d) of Section 250 of the Revenue Act of 1921, Elmer D. Bryson, of Walla Walla, Wash., and the Commissioner of Internal Revenue, hereby consent to a determination, assessment, and collection of the amount of income, excess-profits, or war-profits taxes due under any return made by or on behalf of the said Bryson-Robison Corporation for the years 1917 under the Revenue Act of 1921, or under prior income, excess-profits, or war-profits tax Acts, or under Section 38 of the Act entitled "An Act to provide revenue, equalize duties, and encourage the industries of the United States, and for other purposes", approved August 5, 1909, irrespective of any period of limitations.

This waiver will be effective only one year from date of signing.

(BRYSON-ROBISON CORPORATION)

ELMER D. BRYSON

Taxpayer as former Secretary—

Bryson-Robison Corp.

By D. H. BLAIR

Commissioner.

x

x

If this waiver is executed on behalf of a corporation, it must be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition to which, the seal, if any, of the corporation must be affixed. [99]

[Endorsed]: U. S. Board of Tax Appeals, Div. 15, Docket 22184. Admitted in evidence Jun. 2, 1930. Resp. Exhibit F.

Trans. to Spec Assess 2-11-24

Internal Revenue Income [illegible]

1924 Feb 12 AM 9 27

Distribution Gen Feb 12 1924

Misscellaneous Section

5

COSPER ACCOUNTING COMPANY

Public Accountants Income Tax Advisers
Offices 202 Central Building
206 Farmers and Merchants Yakima, Washington
Bank Building
Walla Walla, Washington
With
Weatherford Wallace Co.
Dayton, Washington

Walla Walla, Washington
February 7, 1924

Commissioner of Internal Revenue
Washington, D. C.

Dear Sir:

In answer to your letter of recent date: symbols:
IT:CA:Ms,2506,WHS-App, to:

BRYSON ROBISON CORPORATION

c/o Elmer D. Bryson

Walla Walla, Washington

we submit herewith the following appeal, duly
signed by Elmer D. Bryson, former secretary of

the above corporation which is now defunct, as requested by your office.

This appeal is made against the findings as contained in your letter of December 19, 1923 as well as those of the Revenue Agent, as contained in his report covering his examination of this corporation for the years 1917, 1918 and 1919.

The particular items in this report that we take exception to, are the elimination from Invested Capital of lands used in the business and the disallowance as an expense, deduction of officer's salaries.

This organization was a corporation in name only, having been conducted thruout its history, as a partnership—composed of two sheep farmers. Absolutely no corporation records or financial records of any kind were kept at any time, prior to the examination by the Revenue Agent. When payments were made to the Stockholders out of funds on hand, they were marked: "Salaries or Dividends", not as a result of any action taken by the officers or stockholders, in the regular way, but just as two farmers would make payments from a fund in which they were equally interested.

The fact that the land used in this business for the purpose of producing feed and range for the sheep was deeded to the individuals composing the corporation was purely a matter of convenience to them. The corporation did not sell this land to the individuals, no consideration having been given. On the other hand, it was not a withdrawal from

the corporation by the individuals as the land continued to be used in the business and was just as much [100] a factor in producing the income as the sheep from which the income was directly derived.

As a matter of fact, county records show that those sheep were assessed to the two individuals separately and were not assessed to the corporation. If the Examining Officer were then to be consistent, he would also eliminate the sheep from the Invested Capital and if that were done, it would be necessary to eliminate the income from the corporation for the reason that the income was derived from the sheep and the land.

It will be noted that the taxes paid on this land have been taken as an allowable deduction by the Examining Officer in determining net income for all years. This is as it should be and in our opinion further substantiates our contention that the land was a part of the Invested Capital of the Corporation and was used in its business. The mere fact that title was held by individuals would certainly not exclude the property from the corporations investment.

These details are given to show that this corporation was not conducted as a corporation, nor in a business-like manner as corporation business might usually be conducted, but as stated above was treated for all practical purposes as a partnership.

Therefore, if the Department is to be consistent and equitable, we feel that the salaries as set up in

our claim; that is \$5,000.00 for the year 1917—\$10,000.00 for 1918 and \$2,500.00 for 1919 as the corporation operated only a part of the year 1919, as shown by the Examining Officer's report, should be allowed these partners and that the total assets used in the business should be permitted in the Invested Capital.

In addition to this, claim is hereby made for Special Assessment for the year 1917 under Section 210 of that law and under Sections 327 and 328 of the 1918 law for the years 1919 and 1918. In the event that it is necessary and you should so desire, we will be glad to set up these claims for Special Assessment separate and apart from this protest.

The Bryson-Robison Corporation was incorporated under the laws of the State of Washington in October 1916 but did not commence operations until 1917. It became defunct in June of 1919 and was stricken from the Corporation rolls at that time.

This protest and appeal is not taken for the purpose of delay.

Respectfully submitted,

BRYSON ROBISON CORPORATION

By Elmer D. Bryson, Formerly Sec.

EM:s

[101]

Subscribed and sworn to before me this the 7th day of February 1924.

[Seal]

ESTHER B. MURRAY

Notary Public in and for the State of Washington,
Residing in Walla Walla. [102]

[Endorsed]: U. S. Board of Tax Appeals, Div. 15, Docket 22184. Admitted in evidence Jun 2, 1930. Respondent's Exhibit G.

Internal Revenue Agent

Jul 1, 1924

Rec'd. Seattle Division

Walla Walla, Washington,

June 30, 1924.

Internal Revenue Agent in Charge,

Seattle Division,

Seattle, Washington.

Sir:—

There is hereby submitted and filed objections and protest to the report to the Commissioner of Internal Revenue from your office, bearing file identifications 4318-W IT:CA-2558-10 Bryson-Robison Corporation.

I

The report adopts the report of Internal Revenue Agent Frank Johnson, eliminating from deductions for invested capital the corporation's entire investment in real estate simply because the bare legal title thereto was transferred to Lester Robison and Elmer D. Bryson. This action is arbitrary and is not justified by the actual facts. This land remained the property of the corporation until June 4, 1919. While record holding of title is *prima facie* evidence of ownership it is in no possible sense conclusive. Every person in interest in this matter concedes as a matter of absolute fact that this land belonged to the corporation except the

Internal Revenue agents. And as invested capital clearly should be clearly taken into account in arriving at the actual deductions to be made in computing the amount of tax. Taxes on the real estate have been passed by you as proper deductions.

If you are going to abide by your conclusion based solely upon the record title to the land you cannot consistently stop there but you must likewise eliminate from the corporate assets the sheep and livestock, which, although actually the property of the corporation, never was of record ownership by the corporation and was assessed and handled of record as the individual properties of Robison and Bryson. When you carry it to this logical conclusion the corporation had no income whatsoever as the total income was from the live stock investment.

II.

There is not a corporation carrying on business of the volume and character this corporation was, requiring the close personal attention, skill and services of a managing head, but that pays a substantial salary for that service. A deduction for salary was claimed for Elmer D. Bryson of \$5000.00 per year, the corporation by whom he was employed was satisfied that his service was worth that amount and paid it to him, [illegible] it is clearly an item which should be allowed as a deduction. [103]

Objections and exceptions and protest have heretofore been filed in this matter and all of the matters and things alleged and set up as objections and protests to your report are hereby, by reference, incorporated in and made a part of this protest and

these objections the same as if annexed hereto or incorporated herein.

Respectfully submitted,
BRYSON-ROBISON CORPORATION,
Elmer D. Bryson
Formerly Secretary. [104]

[Endorsed]: U. S. Board of Tax Appeals, Div. 15, Docket 22184. Admitted in evidence Jun 2, 1930. Respondent's Exhibit H.

[Stamp illegible]

605 Boyer Avenue,
Walla Walla, Washington.
April 18, 1924.

COLLECTOR OF INTERNAL REVENUE,
Tacoma, Washington.
Sir

Re: Bryson-Robison Corporation.

Yours of the 7th inst. is just this day received. This is the busy season in the sheep business and the writer just today returned to this city from shearing operations,—which fact alone accounts for the seeming delay in granting the attention requested in your letter.

You will find herein the claim for abatement, as suggested, and I am very sorry this delay has occurred, but it was beyond my control as I was not in and could not attend to it at the ranch, and I have received your letter.

Very truly,
ELMER D. BRYSON
Formerly Secretary of the
Bryson-Robison Corporation. [105]

[Endorsed]: U. S. Board of Tax Appeals, Div. 15, Docket 22184. Admitted in evidence Jun 2, 1930. Respondent's Exhibit H.

EWB

378

Copy

NES 4-24-24

Dup cl-orig 4-19-24

Collector's Notation

District

Account number

Date received

Stamp here

Collector of Internal Revenue

Treasury Department

Internal Revenue Service

Form 843—Jan., 1922

Comptroller General U. S.

January 18, 1922

CLAIM FOR

- ☒ Abatement of Tax Assessed
- ☐ Credit Against Outstanding Assessments
- ☐ Refund of Taxes Illegally collected
- ☐ Refund of Amounts Paid for Stamps

Used in Error or Excess

[Notice to Collector—Collector must indicate in block above the kind of claim, except in Income Tax cases.]

[Important—File with Collector of Internal Revenue where assessment was made. Not acceptable unless completely filled in.]

[Date received by Administrative Unit—Stamp here.]

State of Washington

County of Walla Walla—ss.

[Type or Print]

BRYSON-ROBISON CORPORATION

(Name of taxpayer or purchaser of stamps.)

Walla Walla, Washington

(Residence—give street and number as well as
city or town and State)

Same 1916-1917

(Business address.)

This deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named, and that the facts given below with reference to said statement are true and complete:

Period	Year
From: October	1916
To: June 4	1919

1. Business in which engaged

Sheep and Livestock

2. Character of assessment or tax

Additional Income

(State for or upon what the tax was assessed
or the stamps affixed.)

3. Amount of assessment or stamps

purchased\$.....

4. Reduction of Tax Liability re-

quested (Income and Profits Tax).....\$.....

5. Amount to be abated\$ 5896.86^v

6. Amount to be refunded (or such

greater amount as is legally re-
fundable)\$.....

7. Dates of payment (see Collector's receipts or indorsements of cancelled checks)
(If statement covers income tax liability, items 8-11, inclusive, must be answered.)
8. District in which return (if any) was filed Washington
9. District in which unpaid assessment appears Washington
10. Amount of overpayment claimed as credit\$.....
11. Unpaid assessment against which credit is asked; period from.....to.....\$.....

Deponents verily believes that this application should be allowed for the following reasons:

This corporation has had no notice of nor has it knowledge of the basis of computation of the above proposed additional tax.

The same is objected to and it's abatement is sought on the grounds and for the reasons assigned and set up in the company claim or specification of objections to the proposed assessment at and about the time of the appeal, reference to which is hereby made and the same, and all thereof, is hereby by reference made a part hereof as fully to all intents and purposes as if herein incorporated.

The levy and basis of arriving thereat, if in conformity with the report to the Commissioner by the Field Auditor is unjust, inequitable and based on false and erroneous assumptions of fact not borne out by the actual, proven facts involved.

This notice, accompanying this blank, was dated at Washington, D. C. March 20th but was received but the 1st of this month, and is being returned within ten days from receipt thereof.

(Attach additional sheets if necessary.)

Signed: ELMER D. BRYSON √ Q2

Formerly Secretary of the
Bryson-Robison Corporation, Inc.

Apr. 16, 1924 √

Sworn to and subscribed before me this 5th day of April, 1924.

[Seal]

HERBERT C. BRYSON

Notary Public for Washington, residing at Walla
Walla, in said state.

(Title.)

(This affidavit may be sworn to before a Deputy
Collector of Internal Revenue or Revenue Agent
without charge.) [106]

To Whom Sold or Issued.	Kind.	Number.	Denomination.	Date of sale or issue.	Amount.	Serial number.	If special tax stamp, state: Period commencing
				\$			
Collector..... District.....							
District							
(Nature of tax.)							
Claimant							
Address							
	Examined and submitted for action, 19.....						
	Committee on Claims						
Amount claimed	\$.....						
Amount allowed	\$.....						
Amount rejected	\$.....						
Claim examined by —	.....					
Claim approved by—	..... Chief of Division.						
Schedule No.	.....					
	Claim No.						

[107]

[107]

CC

1924 Apr 11 AM 10 49

Internal Revenue

Walla Walla, Washington

Central Mail Room

April 5, 1924.

Commissioner of Internal Revenue,
Washington D. C.

Sir:—

RE your IT:CA 2558-WHS

Bryson-Robison Corporation

Your letter of the 20th ult was received by the writer on about the 1st. Inst. and due to the fact of my being very busy in the country was unable to get in to make out a claim for abatement of this proposed additional tax before now, and am doing so, however, within 10 days from receipt thereof.

I have had not the slightest information as to the basis of computation of the amount arrived at, and know and honestly feel a rank injustice is being perpetrated by the attempted imposition of the additional tax. You will find herein claim for abatement, and if for any reason the same is not in proper form I will request the courtesy of being so advised that I may have the same placed in proper form, to the end that it be fairly considered on it's merits.

Very truly,

ELMER D. BRYSON

Formerly Secretary of

Bryson-Robison Corporation. [108]

25 - Rec'd. - 61

(1283)

Apr. 23, 1924

Dist. - Washington

Apr. 16, 1924

IT:R:CC

Collector of Internal Revenue, Wash. District.

The attached claim is returned to you with the request that it be corrected as checked below, so that it will be filed in accordance with the provisions of law and other requirements, as indicated.

- ✓ Claim was received in this office direct from the taxpayer or through your office without being stamped as to date of receipt.
- ☐ Claim should be sworn to before a Deputy Collector, notary public, or other officer authorized to administer oaths. See Articles 1032, 1034, and 1036 of Regulations 62.
- ☐ Claim should be signed by the claimant or his agent. If signed by an officer of a corporation, title of such officer should be shown. If signed by an agent of the taxpayer, a power of attorney must accompany the claim. In the case of the taxpayer's death, certified copies of the letters of administration, letters testamentary, or other similar evidence must be annexed to the claim, to show the authority of the administrator or executor. See Article 1036 of Regulations 62 and A&C Mim. 3097 (the latter relating also to trustees, guardians, and receivers).
- ☐ The basis of the claim must be fully stated. See Articles 1032, 1034, and 1036 of Regulations 62.
- ☐ The year involved and the amount claimed must

be stated. Action may be expedited by filing separate claims for each year.

☐ Claim should be submitted on Form 843. See Article 1031 (a) of Regulations 62.

Paragraph.....of A&C Mim.....
not complied with.

Respectfully,
J. G. Bright,
Deputy Commissioner.
By W. T. Sherwood
Head, Records Division. [109]

[Endorsed]: U. S. Board of Tax Appeals, Div. 15, Docket 22184. Admitted in evidence Jun. 2, 1930. Respondent's Exhibit I.

EWB

Mar-24-4-17

70988

[Date received by Administrative Unit, stamp here]

Recorded [illegible] May 6, 1924. Claims Control Section.

378

Wash 1916-19

[Received—Collector of Internal Revenue, District of Washington, Apr. 19, 1924, Tacoma Office.]
NES 4-21-24—5 8/6.86.

Collector's Notation

District—Washington

Account number—Mar. 04 Spl 17-1924

Date Received—

Stamp here—Burns Poe

Collector of Internal Revenue.

Treasury Department
Internal Revenue Service
Form 843—Jan., 1922
Comptroller General U S.
January 18, 1922

CLAIM FOR

- ☒ Abatement of Tax Assessed
- ☐ Credit Against Outstanding Assessments
- ☐ Refund of Taxes Illegally Collected
- ☐ Refund of Amounts Paid for Stamps

Used in Error or Excess

[Notice to Collector—Collector must indicate in block above the kind of claim, except in Income Tax cases.]

[Important—File with Collector of Internal Revenue where assessment was made. Not acceptable unless completely filled in.]

State of Washington,
County of Walla Walla—ss.

[Type or Print]

BRYSON-ROBISON CORPORATION

(Name of taxpayer or purchaser of stamps.)

Walla Walla, Washington

(Residence—give street and number as well as city or town and State)

Same

(Business address)

This deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named, and that the facts

given below with reference to said statement are true and complete:

Period	Year
From: Oct.	1916
To: June 4	1919

1. Business in which engaged Sheep Raising
2. Character of assessment or tax
(State for or upon what the tax was assessed or the stamps affixed.)
3. Amount of assessment or stamps purchased\$.....
4. Reduction of Tax Liability requested (Income and Profits Tax) \$.....
5. Amount to be abated\$ 5896.86^v
6. Amount to be refunded (or such greater amount as is legally refundable)\$.....
7. Dates of payment (see Collector's receipts or indorsements of canceled checks)
(If statement covers income tax liability, items 8-11, inclusive, must be answered.)
8. District in which return (if any) was filed Tacoma, Washington
9. District in which unpaid assessment appears Tacoma, Washington
10. Amount of overpayment claimed as credit\$.....
11. Unpaid assessment against which credit is asked; period from.....to.....\$.....

Deponent verily believes that this application should be allowed for the following reasons:

Said tax, levied as "additional 1917 Income Tax", is inequitable and unjust, based, as it is on grossly erroneous assumptions of fact by the Auditor; all the actual taxable income for the year 1917 was duly, regularly and properly paid; the basis of arriving at this so-called "additional tax" has never been communicated to the tax-payer. The reasons are also more fully and specifically set out in the exceptions to the Auditor's report on file with the Commissioner of Internal Revenue, and are by reference included herein as fully, to all intents and purposes as if herein set out. No allowance as invested capital is made for large values of real estate claimed to have been in fact owned by the company.

A matter of common fairness would impel the corporation being informed as to the basis of determining this outlandish additional tax, and an opportunity afforded to explain any errors that must exist in the computation, as the tax is grossly wrong.

(Attach additional sheets if necessary.)

Signed: ELMER D. BRYSON

Formerly Secretary of

Bryson-Robison Corporation.

Sworn to and subscribed before me this 18th day of April, 1924.

[Seal]

HERBERT C. BRYSON

Notary Public for Washington, residing at Walla Walla, in said state. (Title)

(This affidavit may be sworn to before a Deputy Collector of Internal Revenue or Revenue Agent

Schedule No. _____ Claim No. _____
 Schedule No. _____ Claim No. _____

CERTIFICATES

I certify that an examination of the records of the Bureau of Internal Revenue shows the following facts as to the assessment and payment of the tax:

Name of Taxpayer.	Character of assessment and period covered.	List.	Year.	Month.	Page.	Line.	Amount	Date Paid	District in which paid.
							\$		

Collector of Internal Revenue

Assessment Clerk, Commissioner's Office

I certify that the records of my office show the following facts as to the purchase of stamps:

To Whom Sold or Issued.	Kind.	Number.	Denomination.	Date of sale or issue.	Amount.	Serial number.	If special tax stamp, state: Period commencing.
					\$		
<div style="display: flex; justify-content: space-between;"> <div> <p>Schedule Number</p> <p>Allowed or Rejected Number</p> </div> <div> <p>Collector</p> <p>District</p> </div> </div>							
<div style="display: flex; justify-content: space-between;"> <div> <p>Claimant</p> <p>Address</p> </div> <div> <p>Examined and submitted for action</p> <p>Committee on Claims</p> </div> </div>							
<p>Amount claimed \$</p> <p>Amount allowed \$</p> <p>Amount rejected \$</p>							
<p>Claim examined by —</p> <p>Claim approved by —</p>							
							[111]

[111]

[Endorsed]: U. S. Board of Tax Appeals. Div. 15. Docket 22184. Admitted in evidence Jun. 2, 1930. Petitioner's Exhibit 1.

99941

THE GRANTORS Lester L. Robison and Elsie Robison, husband and wife, and Bryson-Robison Corporation, a Washington Corporation, for and in consideration of the sum of Ten Dollars and other sufficient valuable considerations in hand paid, convey and warrant to Elmer D. Bryson, the following described real estate in Walla Walla County, Washington, to-wit:

All of sections Three, five, Nine and Eleven, the Northwest quarter of Section Two; The northeast quarter of section four; All of section Fifteen except the southeast quarter thereof; All of the North half of section Fourteen excepting the Southeast quarter of the Northeast quarter thereof; All of section Seventeen except the South half of the Southeast quarter thereof; All of section twenty one lying north of the Oregon-Washington Railroad & Navigation Company's right of way as now laid out and located; All of the West-half Section Twenty-two lying North of said railroad right of way; Also the watering place in said section twenty-two south of said right-of-way as conveyed by George E. Lambdin to Bryson-Robison Corporation. All of the aforesaid lands being in Township seven North of Range 32 E.W.M., Also, All of Sections Thirteen and twenty five in Township Eight North Range 31 E.

W.M., ALSO, All of Sections Seventeen, Nineteen, Twenty-one, Twenty-five, Twenty-seven, Twenty-nine, Thirty-one, Thirty-three, Thirty-five; All of Section Eighteen excepting the southwest quarter thereof; The Northwest quarter, and South half of South half of Section twenty; the Southwest quarter of Section Twenty-two; the west half of the west half of Section Twenty-eight; the Southeast quarter of Section thirty-two; the northwest quarter of the southwest quarter of the Northeast quarter of Section Thirty-four, the last described tract being the 10 acres on which the drilled well is located. All of the lands described in this paragraph being in Township Eight North of Range 32 E.W.M. Dated this 4th day of June A. D. 1919.

BRYSON-ROBISON CORPORATION Inc.,

By LESTER L. ROBISON

President.

By ELMER D. BRYSON

Secretary.

L. L. ROBISON [Seal]

ELSIE ROBISON [Seal]

Forty Dollars United States

Internal Revenue Stamps Cancelled

\$40.00

BRYSON-ROBISON CORPORATION,

Incorporated Oct. 13, 1916.

Walla Walla, Wash.

Attest:

Corporate Seal

State of Washington,
Walla Walla County.—ss.

I, the undersigned, a Notary Public in and for said County and State do hereby certify that on June 4th A. D. 1919, personally appeared before me Lester L. Robison and Elsie Robison, his wife, and L. L. Robison as President and Elmer D. Bryson, as Secretary, respectively, of Bryson-Robison Corporation and acknowledged to me that they and each of them executed the foregoing instrument freely and voluntarily for the uses and purposes therein mentioned; And the said L. L. Robison and Elmer D. Bryson, as such president and secretary respectively of the said corporation acknowledged to me that they executed the instrument as the free and voluntary act of the Corporation and each on oath stated to me that the seal affixed is the corporate seal of the Bryson-Robison Corporation by them thereunto lawfully and authoritatively affixed.

IN TESTIMONY THEREOF I have hereunto set my hand and official seal the date last herein above written.

MARVIN EVANS

Notary Public for Washington
Residing at Walla Walla therein.

Marvin Evans

Notary Public

Commission expires Mar. 26, 1923

State of Washington [112]

Filed for Record June 5th A. D. 1919, at 1:10
P. M., By H. C. Bryson.

GUY ALLEN TURNER

County Auditor

Book 146, page 333 [113]

AUDITOR'S CERTIFICATE OF
CERTIFIED COPY

State of Washington,
County of Walla Walla—ss.

I, Jim L. Reavis do hereby certify that I am the Auditor of Walla Walla County, Washington, and am the legal custodian of such records as are by law required to be kept in the Auditor's office.

That the foregoing is a true and correct copy and transcript of a Deed from L. L. Robison et ux et al to Elmer D. Bryson et ux which was on the 5th day of June, 1919 at the hour of 1 o'clock and 10 minutes P. M., of said day, filed for record in the aforesaid office, and is now of record in said office, on Page 333 Book 146 of Deed Records of Walla Walla County, Washington.

IN TESTIMONY WHEREOF, I have hereunto set my hand and affixed my official seal this 20th day of May at the hour of 3:45 o'clock and..... minutes P. M.

[Seal]

JIM L. REAVIS,

Auditor of Walla Walla, County, Washington

By Frances Lux,

Deputy [114]

CERTIFICATE

United States of America,
State of Washington,
County of Walla Walla.—ss.

I, John L. Sharpstein, sole presiding judge of the Superior Court for Walla Walla County, Washington, the same being a court of record and having an official seal, do hereby certify that the attestation of the annexed document by Jim L. Reavis, County Auditor for Walla Walla County, Washington, is in due form and by the proper officers, and that said Auditor is the official custodian of the original records and files from which said certified copies would be prepared.

JOHN L. SHARPSTEIN,

Superior Judge.

State of Washington,
Walla Walla County.—ss.

I, Walter Kimmerly, County Clerk and ex officio Clerk of the Superior Court for said county and state, do hereby certify that John L. Sharpstein, who executed the foregoing certificate is duly commissioned and qualified as the sole presiding judge of the Superior Court of the State of Washington for Walla Walla County, and that said court is a court of record with an official seal.

WITNESS by hand and the seal of said Superior Court at Walla Walla, Washington, May 20, 1930.

[Seal]

WALTER KIMMERLY,

County Clerk.

By

Deputy [115]

[Endorsed]: U. S. Board of Tax Appeals. Div. 15. Docket 22184. Admitted in Evidence Jun. 2, 1930. Petitioner's Exhibit 2.

THIS INDENTURE, Made the fourth day of June in the year of our Lord one thousand nine hundred and Nineteen between Elmer D. Bryson and Charlotte M. Bryson, his wife, parties of the first part, and L. L. Robison, party of the second part,

WITNESSETH, That the said part..... of the first part, for and in consideration of the sum of Seventy thousand and no/100 Dollars, lawful money of the United States, to them in hand paid, do grant, bargain, sell, convey and confirm unto the said party of the second part, and to his heirs, successors and assigns forever, all those certain pieces or parcels of Real Estate situated in the County of Walla Walla and State of Washington, and more particularly described as follows, to-wit:

All of sections three, five, nine and eleven; the northwest quarter of section two; the northeast quarter of section four; all of section fifteen except the southeast quarter thereof; all of the north half of section fourteen excepting the southeast quarter of the northeast quarter thereof; all of section seventeen except the south half of the southeast quarter thereof; all of section twenty one lying north of the Right of way of the Oregon Washington Railroad & Navigation Company's; all of the west half of section 22 lying north of said O-W. R. & N. Company's right of way; also the watering place in said section 22 lying south of the said railroad right of way

as conveyed by George E. Lambdin to Bryson Robison corporation, all the above lands being in Township 7 N. R. 32 E. W. M. also all of sections thirteen and twenty five in Township 8 N. R. 31 E. W. M.

Also, all the following described lands located in Township 8 N. R. 32 EWM., to-wit:

All of sections seventeen, nineteen, twenty one, twenty five, twenty seven, twenty nine, thirty one, thirty three, thirty five, and all of section eighteen except the southwest quarter thereof; also, the northwest quarter, the south half of the south half of section twenty; the southwest quarter of section twenty two; the west half of the west half of section twenty eight; the southeast quarter of section thirty two; the northwest quarter of southwest quarter of Northeast quarter of section thirty four,—the latter being the 10 acre tract on which the drilled well is located.

together with all and singular the tenements, hereditaments and appurtenances thereunto belonging or in anywise appertaining, together with the rents, issues and profits of said premises, and the parties of the first part, for themselves and their heirs and assigns, covenant and agree that they are the owners of said Real Estate and have fee simple title thereunto.

This conveyance is intended as a MORTGAGE to secure the payment of the sum of Seventy thousand no-100 Dollars, which sum is represented by one promissory note of even date herewith, substantially of the tenor and effect following, to-wit:

COPY OF NOTE

\$70,000.00

Walla Walla, Washington, June 4, 1919.

October 15th, 1921, on or before, after date, without grace, for value received, I promise to pay L. L. Robison or order, at the Baker Boyer National Bank of Walla Walla, Washington Seventy Thousand Dollars in gold coin, with interest thereon in like coin from date until paid at the rate of six per cent per annum, interest payable [116] annually, if not so paid, to draw interest until paid, at the same rate as the principal. In case action is brought to collect this note, I agree that the venue of such action may be laid in Walla Walla County, Washington, and that the action may be there maintained without regard to the residence of the defendants, and that in any action brought hereupon I will pay such sum as the court may adjudge reasonable as attorneys fees. Any part payable at any time.

ELMER D. BRYSON

CHARLOTTE M. BRYSON

(\$14.00 Internal Revenue stamps affixed and cancelled).

Said note is executed by the said parties of the first part, payable to the said party of the second part at The Baker Boyer National Bank in Walla Walla, Wash., in U. S. Gold Coin, together with interest thereon in like coin, from date until paid at the rate of 6 per cent. per annum, payable annually, and if not so paid, the interest to draw interest at the same rate as the principal, or if not so paid the whole indebtedness hereby secured may,

at the option of the holder, become at once due and payable, and further provide for the payment of such sum as the Court may adjudge reasonable as attorney's fees in case action or suit be brought to collect the whole or any part of said note, and in case of foreclosure, that if the mortgaged property shall not upon sale realize sufficient to pay said principal and interest in full, together with the costs and expenses of such foreclosure, a deficiency judgment may be rendered for such unpaid balance.

And mortgagor further covenant and agree to keep all buildings on said premises fully insured at all times against loss or damage by fire or other elements, in some safe and reliable insurance company, loss, if any, payable to second part..... or assigns.

And the parties of the first part covenant and agree to pay said note according to the terms thereof, and further covenant and agree that in the event of the foreclosure of this mortgage and the sale of the mortgaged property aforesaid, there shall not be realized sufficient to pay the judgment, principal, interest and costs, a deficiency judgment may be rendered against them for any unpaid balance, and that execution may be issued for the collection thereof and levied upon any property belonging to the makers of this mortgage not exempt from execution. And the parties of the first part further covenant and agree to pay all taxes or other assessments that may be assessed or levied on the said mortgaged premises before the same become delinquent, and to pay all taxes or other assessments that may here-

after be assessed or levied on this mortgage or the indebtedness secured thereby, and in case of failure to so pay said taxes or other assessments or any part thereof the party of the second part may pay the same and add the sum so paid to the demand hereby secured, and to bear the same rate of interest; and these presents shall be void if all such payments be made. But in case default be made in the payment of principal or interest, as in said note provided, or the parties of the first part shall fail to keep and perform each and every covenant and agreement herein contained, on their part, then in either event the said part..... of the second part his heirs, successors or assigns is hereby empowered to foreclose this mortgage and sell the said mortgaged premises, with all and every the appurtenances, or any part thereof, in the manner prescribed by law; and out of the money arising from such sale to retain the said principal and all interest up to the time of such sale, and all sums paid for taxes or other assessments on said premises, or said note or mortgage, together with the costs and charges of such foreclosure and of making such sale, and such additional sum as the Court may adjudge reasonable as attorney's fees in such action or suit, which the parties of the first part, agree to pay in case action or suit is instituted to foreclose this mortgage; and the overplus, if any there be, shall be paid by the party making such sale, on demand, to the said parties of the first part their heirs or assigns. [117]

IN WITNESS WHEREOF, The said parties of

the first part have hereunto set their hands and seals
the day and year first above written.

ELMER D. BRYSON (Seal)

CHARLOTTE M. BRYSON (Seal)

Signed, sealed and delivered in presence of

HERBERT C. BRYSON.

State of Washington,
County of Walla Walla—ss.

I, the undersigned, a Notary Public in and for the
State and County aforesaid, do hereby certify that
on this 4th day of June A. D. Nineteen Hundred
and Nineteen personally appeared before me Elmer
D. Bryson and Charlotte M. Bryson, husband and
wife, whose name *is* subscribed to the foregoing in-
strument, to me personally known to be the same
persons described in and who executed the said in-
strument, and acknowledged to me that they each
signed, sealed and executed the same freely and
voluntarily for the uses and purposes therein ex-
pressed.

IN TESTIMONY WHEREOF, I have hereunto
set my hand and affixed my official seal this the day
and year in the certificate above written.

[Seal]

HERBERT C. BRYSON,

Notary Public for the State of Wash-
ington, residing at Walla Walla, Wash.

Notary Public

Herbert C. Bryson

Commission expires

Dec. 20, 1920.

State of Washington

Filed for record this 10th day of June, 1919 at
1:40 P. M. at the request of Evans and Watson.

GUY ALLEN TURNER,
County Auditor.

Vol. 114, page 4 [118]

CERTIFICATE

United States of America,
State of Washington,
County of Walla Walla.—ss.

I, John L. Sharpstein, sole presiding Judge of
the Superior Court for Walla Walla County, Wash-
ington, the same being a court of record and having
an official seal, do hereby certify that the attestation
of the annexed document by Jim L. Reavis, County
Auditor for Walla Walla County, Washington, is in
due form and by the proper officers, and that said
Auditor is the official custodian of the original rec-
ords and files from which said certified copies would
be prepared.

JOHN L. SHARPSTEIN,
Superior Judge.

State of Washington,
Walla Walla County.—ss.

I, Walter Kimmerly, County Clerk and ex officio
Clerk of the Superior Court for said county and
state, do hereby certify that John L. Sharpstein,
who executed the foregoing certificate is duly com-
missioned and qualified as the sole presiding judge
of the Superior Court of the State of Washington

for Walla Walla County, and that said court is a court of record with an official seal.

WITNESS my hand and the seal of said Superior Court at Walla Walla, Washington, May 20, 1930.

[Seal]

WALTER KIMMERLY,

County Clerk

By

Deputy [119]

State of Washington,

County of Walla Walla.—ss.

I, Jim L. Reavis, do hereby certify that I am the duly elected, qualified and acting Auditor of Walla Walla County, Washington, and am the legal custodian of such records *are* are by law required to be kept in the Auditor's office.

I certify that the foregoing is a true and correct copy and transcript of a real estate mortgage from Elmer D. Bryson et ux to L. L. Robison which was on June 10, 1919, at 1:40 p. m. filed for record in the aforesaid office, and is now of record in my office on page 4, Vol. 114 of Real Estate mortgage records for Walla Walla County, Washington.

I further certify that said real estate mortgage bears a marginal release, written on the margin of the official record thereof by L. L. Robison, mortgagee, dated Aug. 5, 1921, showing the same to be fully paid, satisfied, released and discharged of record, as authorized by § 11604 of Remington's statutes of Washington.

IN TESTIMONY WHEREOF I have hereunto

set my hand and affixed my official seal at Walla Walla, Washington, May 20, 1930.

JIM L. REAVIS

Auditor of Walla Walla County,
Washington.

By

Deputy. [120]

[Endorsed]: U. S. Board of Tax Appeals. Div. 15.
Docket 22184. Admitted in Evidence Jun. 2, 1930.
Petitioner's Exhibit 3.

PROOF OF PUBLICATION

13959

State of Washington,
County of Walla Walla.—ss.

E. G. Robb, being first duly sworn upon oath, deposes and says: I am the publisher of the Walla Walla Union, a daily newspaper. which is now, and for the last past nine months and more has been established, printed, published and circulated continuously as a daily newspaper in the City of Walla Walla, in the county and state aforesaid, and of general circulation in said city, county and state.

The Notice, of which the one hereto attached is a full, true and correct copy, was published in said newspaper once each week for 8 consecutive weeks, being published therein 8 times, the first publication being on the 22nd day of March, 1920, and the last publication being on the 10th day of May, 1920.

Said notice was published in the regular and entire issue of said newspaper during the said period and times of publication and was published in said newspaper proper and not in any supplement thereof.

E. G. ROBB

Sworn to and subscribed before me this 10th day of May, 1920.

[Seal]

D. W. IFFT

Notary Public in and for the State of Washington,
Residing at Walla Walla, Washington.

Filed May 14, 1920.

E. J. BRUNTON, Clerk.

By C. R. Portch,

Deputy. [121]

NOTICE OF HEARING

In the Superior Court of the State of Washington
In and for the County of Walla Walla.

In the Matter of the Dissolution
of

The Bryson-Robinson Corporation

Notice is hereby given that pursuant to a resolution of the stockholders of the Bryson Robinson Corporation at a meeting held on the 22nd day of April, 1919, called for the purpose of dissolving and disincorporating said corporation, adopted by a unanimous vote of all of the stock of said corporation to dissolve and disincorporate the same, an application has been filed in the Superior Court of the State of Washington, for Walla Walla County

to dissolve and disincorporate said corporation and notice is hereby given that on Monday the 18th day of May, 1920, at 10 o'clock A. M. on said day at the court room of the Superior Court of the state of Washington, for Walla Walla County, hearing upon said application will be had and the Court will proceed to dissolve and disincorporate said corporation if it shall appear that the said corporation has taken the necessary preliminary steps and obtained the necessary vote to dissolve itself and that all claims against said corporation are discharged.

Witness the Hon. Edward C. Mills, Judge of the said Superior Court, and the seal of said Court hereto affixed this 19th day of March, 1920.

[Seal of the

E. J. BRUNTON

Superior Court]

Clerk of the Superior Court

By C. R. Portch, Deputy.

3—22-29; 4—5-12-19-26; 5—3-10. [122]

NOTICE OF HEARING

In the Superior Court of the State of Washington
In and for the County of Walla Walla.

No. 13959

In the Matter of the Dissolution
of

The Bryson-Robinson Corporation

NOTICE IS HEREBY GIVEN that pursuant to a resolution of the stockholders of the Bryson-Robinson Corporation at a meeting held on the 22nd day of April, 1919, called for the purpose of dissolving and disincorporating said corporation, adopted by a

unanimous vote of all of the stock of said corporation to dissolve and disincorporate the same, an application has been filed in the Superior Court of the State of Washington, for Walla Walla County to dissolve and disincorporate said corporation and notice is hereby given that on Monday the 17th day of May, 1920, at 10 o'clock A. M. on said day at the Court Room of the Superior Court of the State of Washington, for Walla Walla County, hearing upon said application will be had and the Court will proceed to dissolve and disincorporate said corporation if it shall appear that the said corporation has taken the necessary preliminary steps and obtained the necessary vote to dissolve itself and that all claims against said corporation are discharged.

WITNESS the Hon. Edward C. Mills, Judge of said Superior Court, and the seal of said Court hereto affixed this 19th day of March, 1920.

[Seal]

E. J. BRUNTON

Clerk of Superior Court

By C. R. Portch

Deputy.

Filed Mar. 20, 1920.

E. J. BRUNTON, Clerk
by C. R. Portch,

Deputy. [123]

NOTICE OF HEARING.

In the Superior Court of the State of Washington
In and for the County of Walla Walla

In the Matter of the Dissolution
of

The Bryson-Robinson Corporation.

NOTICE IS HEREBY GIVEN that pursuant to a resolution of the stockholders of the Bryson-Robinson Corporation at a meeting held on the 22nd day of April, 1919, called for the purpose of dissolving and disincorporating said corporation, adopted by a unanimous vote of all of the stock of said corporation to dissolved and disincorporate the same, an application has been filed in the Superior Court of the State of Washington, for Walla Walla County to dissolve and disincorporate said corporation and notice is hereby given that on the 20th day of October, 1919, at 10 oclock A. M. on said day at the Court Room of the Superior Court of the State of Washington, for Walla Walla County, hearing upon said application will be had and the Court will proceed to dissolve and disincorporate said corporation if it shall appear that the said corporation has taken the necessary preliminary steps and obtained the necessary vote to dissolve itself and that all claims against said corporation are discharged.

WITNESS, the Hon. Edward C. Mills Judge of said Superior Court, and the seal of said Court

hereto affixed this 24th day of Aug. 1919.

[Seal]

E. J. BRUNTON

Clerk of Superior Court.

By C. R. Portch,

Deputy.

Filed Aug. 24, 1919.

E. J. BRUNTON, Clerk

By C. R. Portch,

Deputy. [124]

PETITION.

13959

In the Superior Court of the State of Washington
for Walla Walla County.

In the Matter of the Dissolution of the
Bryson-Robison Corporation.

To the Honorable Edward C. Mills, Judge of the
Above Entitled Court:

The petition of the Bryson-Robison corporation
respectfully shows:

I.

That the Bryson-Robison Corporation is a corporation duly organized and existing under the laws of the State of Washington, with its principal place of business at Walla Walla, Washington.

II.

That at a meeting of the stockholders of said corporation held on the 22d day of April, 1919, called for the purpose of dissolving and disincorporating

said corporation, it was decided by vote of two-thirds of all the stockholders of said corporation, to-wit: by a unanimous vote of all of said stockholders to dissolve and disincorporate said corporation. That at the said meeting the following resolutions were adopted by the stockholders of said corporation, to-wit:

“BE IT RESOLVED by unanimous vote of the stockholders of the Bryson-Robison Corporation called for the purposes of this resolution that said corporation dissolve and disincorporate, and

BE IT FURTHER RESOLVED that the officers of said corporation be and they hereby are authorized and directed to take the necessary legal steps to disincorporate and dissolve said corporation.

III.

That a certificate duly signed by the President, attested by the Secretary under the seal of the corporation of the minutes and call of said meeting is hereto annexed and marked Exhibit A, and adopted and made a part of this petition. [125]

WHEREFORE Petitioner prays that notice of this application be given by the Clerk of this Court as provided by law and that at the time and place appointed in such notice or at any time to which such hearing may be postponed, an order may be entered declaring the said corporation dissolved and that such other and further order may be made as is meet in the premises.

GOSE & CROWE,

Attorneys for Petitioner.

State of Washington,
County of Walla Walla—ss.

I, Elmer D. Bryson, being first duly sworn on oath say: I am Secretary-Treasurer of the Bryson-Robison Corporation, the petitioner above named; I have read the foregoing petition, know the contents thereof and believe the same to be true.

ELMER D. BRYSON.

Subscribed and sworn to before me this 22d day of April, 1919.

W. F. CROWE,

Notary Public.

Filed in the office of the Clerk of the Superior Court this 24 day of April, 1919.

E. J. Brunton, Clerk

By C. R. Portch deputy. [126]

In the Superior Court of the State of Washington
for the County of Walla Walla.

State of Washington,
County of Walla Walla—ss.

I, Walter Kimmerly, County Clerk of the County of Walla Walla, State of Washington, and ex officio Clerk of the Superior Court of the State of Washington for Walla Walla County, do hereby certify that the within and foregoing are full, true and correct copies of the originals, and of the whole thereof as the same are now on file and of record in the within entitled action in my office and custody.

I further certify that I have carefully examined all of the records and files of said court in the within entitled action and therefrom certify that neither the Commissioner of Internal Revenue, the Collector of Internal Revenue, nor any officer or agent of either of them, nor any other person, firm or corporation, at any time or at all filed in said action or proceeding any objection of any character to the dissolution of said corporation as sought in the petition on file in my office.

IN WITNESS WHEREOF I have hereunto set my hand and affixed the seal of said Superior Court May 21st, 1930.

[Seal]

WALTER KIMMERLY,

County Clerk.

By EDNA BATES,

Deputy.

State of Washington,
County of Walla Walla—ss.

I, John L. Sharpstein, Judge of the Superior Court of the State of Washington, for Walla Walla County, do hereby certify that Walter Kimmerly, whose name is subscribed to the preceding exemplification, is the County Clerk of Walla Walla County and ex-officio Clerk of the Superior Court of said County, and that full faith and credit are due to his official acts.

I further certify that the seal affixed to the exemplification is the seal of our said Superior Court,

and that the attestation thereof is in due form and according to the form of attestation in this State.

JOHN L. SHARPSTEIN,

Judge of the Superior Court.

Dated at Walla Walla, Washington, this 21st day of May, A. D., 1930. [127]

State of Washington,
County of Walla Walla—ss.

I, Walter Kimmerly, County Clerk and ex-officio Clerk of the Superior Court of the State of Washington, for Walla Walla County, do hereby certify that John L. Sharpstein, whose name is subscribed to the preceding certificate, is Judge of the Superior Court of the State of Washington, for Walla Walla County, duly elected, sworn and qualified, and that the signature of said Judge to said certificate is genuine.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of said Superior Court, of Walla Walla, the county seat of said County, this 21st day of May, 1930.

[Seal]

WALTER KIMMERLY,
Clerk of said Superior Court. [128]

[Endorsed]: U. S. Board of Tax Appeals. Div. 15.
Docket 22184. Admitted in Evidence Jun. 2, 1930.
Petitioner's Exhibit 4.

United States of America
State of Washington

DEPARTMENT OF STATE

[The Seal of the State of Washington, 1889]

To All to Whom These Presents Shall Come

I, J. Grant Hinkle, Secretary of State of the State of Washington and custodian of the Seal of said State, do hereby certify that I have carefully examined the records of this office and find that the "BRYSON-ROBISON CORPORATION", a domestic corporation of Walla Walla, Washington, filed a copy of its articles of incorporation in this office on the 13th day of October, 1916.

I further certify that the above mentioned corporation was stricken from the records of this office July 1, 1921, and was further "Stricken from Records and dissolved" July 1, 1924 under the provisions of Chapter 144, Laws of Washington of 1923, for failure to pay the annual license fees and accruing penalties, the last license fee paid being for the fiscal year ending June 30, 1919.

And I further certify that the above mentioned corporation has had no legal corporate existence since stricken July 1, 1921, pursuant to Chapter 140, laws of 1907.

In Testimony Whereof, I have hereunto set my hand and affixed hereto the Seal of the State of Washington. Done at the Capitol, at Olympia, this 14th day of May A. D. 1930.

[Seal]

J. GRANT HINKLE,

Secretary of State.

By A. M. HITTO,

Assistant Secretary of State. [129]

[Endorsed]: U. S. Board of Tax Appeals. Div. 15. Docket 22184. Admitted in evidence Jun. 2, 1930. Petitioner's Exhibit 5.

(Received Aug. 12, 1924. Special Assessment Section.)

[original torn—illegible]

IT:CA

Walla Walla, Washington

January 2nd

(da

1924

INCOME AND PROFITS TAX WAIVER

In pursuance of the provisions of subdivision (d) of Section 250 of the Revenue Act of 1921, Bryson-Robinson, Corporation of Walla Walla, Washington and the Commissioner of Internal Revenue, hereby consent to a determination, assessment, and collection of the amount of income, excess-profits, or war-profits taxes due under any return made by or on behalf of the said Corporation for the years 1917 and 1918 under the Revenue Act of 1921, or under prior income, excess-profits, or war-profits tax Acts, or under Section 38 of the Act entitled "An Act to

provide revenue, equalize duties, and encourage the industries of the United States, and for other purposes'', approved August 5, 1909, irrespective of any period of limitations.

ELMER D. BRYSON

Former Secretary of the Bryson-Robison Corp.

Taxpayer

D. H. BLAIR C

Commissioner

If this waiver is executed on behalf of a corporation, it must be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition to which, the seal, if any, of the corporation must be affixed. [130]

[Endorsed]: U. S. Board of Tax Appeals. Div. 15.
Docket 22184. Admitted in evidence Jun. 2, 1930.
Petitioner's Exhibit 6.

Telephone 7

Herbert C. Bryson

Attorney at Law

312-313 Drumheller Bldg.

Walla Walla, Washington

December 26, 1923

Commissioner of Internal Revenue,

Washington, D. C.

Sir:

Re: Your IT:CA:Ms 2506-WHS-App.

Elmer D. Bryson has handed me your office letter of the 19th inst. addressed to Bryson-Robison Cor-

poration, in his care, advising that it will be necessary for this corporation within twenty days from the date of your letter to advise you of its acquiescence in the determination of net income and invested capital as found by the Revenue Agent's report dated October 22, 1923, in order that you may further consider an application for computation of tax under the provisions of Section 210, Revenue Act 1917 and Sections 327-8, Revenue Act 1918.

You have already been informed that this corporation has been entirely out of business since June 1919, and since that date has not owned or possessed any property of any character and the corporation has long since been stricken from the corporate rolls of this State where it was incorporated. It has not functioned in any manner since that date, and being stricken from the corporate rolls naturally the former officers of the corporation cannot legally presume to act for it since it no longer exists.

During the life of the corporation Elmer D. Bryson was secretary of the corporation, but will not presume to assume to act in that capacity after all of these years since its dissolution. The only way he could make a report would be that as that of an individual, who was formerly secretary of a corporation which has been defunct for a period of over four and one half years, and during which period it has neither functioned nor owned any property.
(Underscoring supplied)

Your office letter above referred to is being by him referred to Cospier Accounting Company, who has been looking after this matter and it will probably give your letter such further attention and reply as it deems proper and necessary. We deemed it proper that this status of affairs should now again be called to your attention, as no former officer will assume an authority not vested in him.

Yours very truly,

HERBERT C. BRYSON [131]

[Endorsed]: U. S. Board of Tax Appeals. Div. 16.
Docket 22184. Admitted in evidence Jun. 2, 1930.
Petitioner's Exhibit 7.

Form 850-A

Revised July, 1924

TREASURY DEPARTMENT

Internal Revenue Service

[Insignia]

Office of

Supervising Internal Revenue Agent

Seattle, Wash.

807 4th Ave.

Oct. 24, 1924

Elmer D. Bryson

605 Boyer Ave.

Walla Walla, Wash.

In re: Income Tax

Date of Report: Oct. 24, 1924

Years examined: 1919, 1920 and 1921

Dear Sir:

There is transmitted herewith copy of a report covering examination recently made by a repre-

sentative of this office covering your income tax liability, and a form of agreement which, if the adjustments suggested are satisfactory to you, you may sign and return to this office. The agreement, however, until approved by the Commissioner, upon a review of the examining officer's report in Washington, is not binding. In the event the report is not approved upon review in Washington and there are material changes, you will be given the benefit of due notice and afforded an opportunity to discuss the changes with this office.

If you do not agree with the conclusions stated in the report, it is desired that every opportunity be afforded you to present any objections or additional information which you believe might affect the result of the final decision of the Commissioner of Internal Revenue at Washington, D. C. The original of this report will, therefore, be held in this office for a period not to exceed twenty days from the date of this letter in order that you may, if you so desire, present any protests, briefs, or letters containing additional information. Such protests, briefs, or letters should be forwarded in triplicate to this office, where they will receive careful consideration before the report with all papers pertaining thereto is transmitted to the Department at Washington for final action. If you agree to the findings of the examining officer the report will be forwarded at once. In the event that you do not submit protest or brief within the twenty-day period, the report will immediately thereafter be forwarded to the Bureau. However, any appeal, protest or additional information affecting the inclosed report should be directed to this office, and not to the Bureau at

Washington. If forwarded to the Bureau direct, it will be referred to this office for appropriate consideration.

No remittance should be made until you receive notice of assessment from the Collector of Internal Revenue for your district.

Please acknowledge receipt by return mail.

Respectfully,

F. H. GOUDY

Supervising Internal Revenue Agent.

By W. A. HOLT

Internal Revenue Agent [132]

TREASURY DEPARTMENT

Internal Revenue Service

[Insignia]

Office of

807 4th Ave.

Internal Revenue Agent

Portland Division

October 24, 1924

No. 7518-W

IT:R:FR

In re: Elmer D. Bryson

605 Boyer Ave.

Walla Walla, Washington

Recommended

Deficiency in Tax Overassessment

1919 No change

1920 \$7.45

1921 No change

Total \$7.45

Commissioner of Internal
Revenue

IT:R For Attention
Head Personal Audit
Division

Enclosed herewith is a report of Internal Revenue Agent Frank Johnson dated July 18, 1924 covering his investigation of the above named individual for the years 1919 to 1921, inclusive indicating a net overassessment of \$7.45, which I recommend be credited or refunded.

The examining officer was instructed to make this investigation in view of your letter of May 7, 1924 IT:R:UR:10-BBC stating the records of your office fail to show the taxpayer filed returns for 1919 and subsequent years.

Returns were filed in the District of Washington on form 1040 for 1919 and 1921 and on form 1040A for the year 1920.

A copy of this report has been mailed to the taxpayer with a request that the receipt of same be acknowledged. A copy of office letter to taxpayer is enclosed.

F. H. GOUDY

Supervising Internal Revenue Agent

By

AFS:KP

Internal Revenue Agent [133]

Treasury Department,
Internal Revenue Service.
Form 845k.
Aug., 1921.
Name ELMER D. BRYSON

SCHEDULE 1

Joint Return—form 1040

Year 1919

BLOCK ADJUSTMENTS

Block	Return	Additions	Reductions	Corrected	Wife's Income
A	\$ 1,516.08	\$14,993.03	\$	\$16,509.11	\$.....
B					
C					
D			18,187.13	(18,187.13)	.....
E					
F					
G					
Total					
H	1,516.08	14,993.03	18,187.13	(1,678.02)	.....
I	20.00			20.00	.....
Total					
J	1,496.08			(1,698.02)	.....
K(a)	247.50	4,857.38		5,104.88	.....
(b)		27.14		27.14	.....
L					
M					
N					
Total	1,743.58	19,877.55	18,187.13	3,434.00	.....
Wife's net income or loss					
Husband's net income xxxxx				3,434.00	

Elmer D. Bryson

SCHED. 1-A

Explanation of Items—Changed

Detail of Income and Expenditures for the year 1919, as shown by Agent's supplemental report covering the Bryson-Robison Corporation. As shown in the report covering the investigation of the corporation, the net income for the entire year was apportioned between the corporation and Elmer D. Bryson for the reason that Mr. Bryson took over all of the assets of the corporation on June 4, 1919 and thereafter conducted the business as an individual, no segregation of the business between the corporation and the individual having been made at the time of change and by reason of overlapping items, and the further reason that neither the corporation or the individual kept any regular books of account, an apportionment of the net income based on the time held by each appears to be an equitable division. [135]

Elmer D. Bryson
SCHED. 1-A (cont.)

Explanation of Items—Changed

Block A.

Sale of Sheep		\$42,777.75
Sales of Wool		27,196.93
Sales of Cattle		150.00
		<hr/>
Total		\$70,124.68
Total amended Inventories 12-31-18		\$37,570.00
No Purchases recorded		
Inventories 12-31-19		
1500 Ewes at \$4.00	\$ 6,000.00	
1700 Sheep at \$8.91	15,147.00	
100 Lambs at 8.15	8,150.00	
Cattle	1,925.00	
	<hr/>	
Total closing inventories		31,222.00
		<hr/>
Difference		6,348.00
		<hr/>
Gross Income from sales		63,776.68
Misc. Income sale of hides		100.00
		<hr/>
Gross Income		\$63,876.68

Elmer D. Bryson

SCHED. 1-A (cont.)

Explanation of Items—Changed

Block A. (cont.)

Gross Income forward		\$63,876.68
Deductions:		
Labor	\$9,271.02	
Supplies & Provisions	2,664.49	
Rent of Pasture	1,559.92	
Gas, Oil & auto Exp.	1,876.49	
Sacks	160.56	
Feed Purchased	9,869.27	
Water	659.07	
Misc. Expense	183.05	
	<hr/>	
12. Total necessary expense	26,243.87	
14. Misc. Repairs	872.61	
15. Interest	1,674.83	
16. Taxes	2,218.18	
18. Depreciation	2,028.42	
	<hr/>	
20. Total deductions		33,037.91
		<hr/>
7. Net income for taxable period		\$30,838.77
Above income apportioned as follows:		
54/365 Attributed to earnings of corporation	\$13,271.57	
11/365 Attributed to earnings of Elmer D. Bryson	17,567.20	
	<hr/>	
Total	\$30,838.77	
Earnings of Elmer D. Bryson with corporation		\$17,567.20
Additional deductions not on corporation books		
State and County Taxes	\$278.18	
Insurance & Interest	46.44	
Expense of Auto in business	143.47	
Depreciation Ex. F'	590.00	
	<hr/>	
Total net income		16,509.11

Elmer D. Bryson
SCHED. 1-A (cont.)

Explanation of Items—Changed

Block D. Nothing is shown in this block in the return filed, the taxpayer sustained a loss in taking over the assets of the corporation as a liquidating dividend, as defined under Article 1548 and 1564 Reg. 45 as amended.

Assets received by Elmer D. Bryson in lieu of Stock held in the Bryson-Robison Corporation.

Sheep Amended Inventory	\$29,297.00
Rams	4,701.39
Real Estate	56,575.15
Farm Bldgs.	5,801.09
Cattle	1,925.00
Pack outfits	8,146.00
Pack horses	415.00

Total	106,860.63
Less Depreciation Reserve	4,426.23

Value of Assets as shown by books of Corp.	\$102,434.40
Assets originally paid in	\$50,621.53
Paid Lester L. Robison	70,000.00
	120,621.53

Net loss	\$18,187.13
----------	-------------

In the above adjustment the corporation's book value is deemed the fair value as at dissolution.

[138]

Block I. Contributions

Y. M. C. A.	\$ 5.00
Red Cross	15.00

Total	\$20.00
-------	---------

Block K-a Dividends were increased by 4,857.38 representing additional earnings of the Bryson Robison corporation to June 4, 1919.

Representing the balance of corporation surplus account after deducting accrued income tax liability as shown by final closing of constructed books for the corporation

Total dividend	\$5,104.88
----------------	------------

Block K-b Interest received on Victory Bond 27.14

[139]

216

Guy T. Helvering vs.

Treasury Department,
Internal Revenue Service.

Form 845.

Aug., 1921

Name ELMER D. BRYSON

SCHEDULE 2

Year ended 12-31-19

NET INCOME

Net income as disclosed by return.....	\$ 1,743.58
As corrected	3,434.00
Net additions	1,690.42

Additions:

(a) Sales of sheep & wool	\$14,993.03
() Dividends increased	4,857.38
() Int. on Victory Bond	27.14
()	
()	
()	
()	

Total additions.....	\$19,877.55
----------------------	-------------

Deductions:

() Net Loss Stock of Corporation.....	\$18,187.13
()	
()	
()	
()	

Total deductions.....	\$18,187.13
-----------------------	-------------

Net additions as above.....	1,690.42
-----------------------------	----------

[140]

Treasury Department,
Internal Revenue Service.

Form 845 m.

Aug., 1921.

Name ELMER D. BRYSON

SCHEDULE 3
COMPUTATION OF TAX

	Year ended 12-31-19
Total net income, Schedule 2	3,434.00
2 dependents\$ 400.00	
specific 2000.00	
Less: Exemption	2400.00
Dividends	5104.88
Interest on U. S. obligations, etc....	27.14 7,532.02
Income subject to Normal Tax.....	none
Tax% on.....	
Tax% on.....	
Tax% on.....	
Tax% on.....	
Surtax husband's income	
Surtax wife's income	
Surtax at prior years' rates	
Excess Profits Tax, Section 201.....	
Excess Profits Tax, Section 209.....	
Total Tax	
Less tax withheld at source (for 1917 not to exceed Normal Tax)	
Taxes, Section 222, 1918 Act	
Total Tax Assessable.....	none
Tax previously assessed	"
Additional tax to be assessed (overassessment)	"

[141]

Treasury Department,
Internal Revenue Service.
Form 845k.
Aug., 1921.

Name ELMER D. BRYSON and CHARLOTTE BRYSON, his wife

SCHEDULE 4

Joint Return Form 1040 A Year 1920

BLOCK ADJUSTMENTS

Block	Return	Additions	Reductions	Corrected	Wife's Income
A	\$ 3,215.55	\$	\$ 7,308.61	\$(4,093.06)	\$.....
B					
C					
D	(700.00)	420.00		(280.00)	.....
E	80.00			80.00	.....
F					
G					
Total					
H	2,595.53	420.02	7,308.61	(4,293.06)	.....
I					
J					
K(a)	9.00			9.00	.....
K(b)					
L					
M					
N		20			.....
Total	2,586.33	420.22	7,308.61	(4,302.06)	.....

Wife's net income or loss.....
Husband's net income or loss..... (4,302.06)

Elmer D. Bryson
 SCHED. 4-A (cont.)

Explanation of Items—Unchanged

Copy of Return filed Form 1040 A Year 1920

Sched. A.	Live Stock sold			\$25,850.95
	Wool sold			25,552.53
	Pelts and sacks			385.60
				<hr/>
	Total			\$51,789.08
	Cost of Rams sold	\$3,225.00		
	Received	500.00		
		<hr/>		
	Loss			2,725.00
				<hr/>
	Gross Income			49,064.08
	Expenses			
	Labor	12,954.74		
	Groceries	5,196.47		
	Feed	14,591.79		
	Water & Freight	1,378.96		
	Land rental	917.07		
	Repairs	1,675.89		
	Gas and Oil	708.06		
	Insurance & taxes	3,244.04		
	Interest	4,631.01		
	Abstracts & Com.	506.50		
	Telephone	25.00		
	Tolls & ferrying	19.00		45,848.53
		<hr/>		<hr/>
	Net Income			3,215.55
Sched. D.	Sale of Real Est. of J. K. Fuller	\$3,500.00		
	Acquired 1914 cost	\$4500.00		
	Deprn.	300.00	4,200.00 loss (700.00)	
		<hr/>	<hr/>	
Sched. E.	Rent Henry Blackman			80.00
				<hr/>
Sched. H.	Total net income			2,595.53*
	Red Cross	4.00		
Sched. K.	Contributions Y.W.C.A.	5.00		9.00
		<hr/>		<hr/>
Sched. N.	Total net income			\$2,586.33**

Elmer D. Bryson

SCHED. 4-A (cont.)

Explanation of Items—Unchanged

Computation of Tax

14. Net Income	\$2,586.33
15. Exemptions 2 Dep.	2,400.00
16. Balance taxable	<u>186.33</u>
17. Tax due at 4%	\$7.45

Interest received on Liberty Bonds \$111.25

*Error in addition 2¢. **Error in subtraction 20¢.

[143]

Elmer D. Bryson

SCHEDULE 4-B

Explanation of Items—Changed

Sched. A.	Wool Sales		\$25,552.53
	Sheep Sales		26,357.51
	Miscl. sales		320.16
	Cattle Sales		<u>1,625.00</u>
	Total		\$53,855.20
	Cattle Inv. 1-1-20	\$ 1,925.00	
Corrected	Sheep Inv. 1-1-20	29,297.00	
	Sheep purchased	<u>2,400.00</u>	
	Total		\$33,622.00
Inv. 4150	sheep @ 5.08 12-31-20	\$21,082.00	
Inv. of	Cattle 12-31-20	<u>300.00</u>	
	Total		<u>21,382.00</u>
	Difference		12,240.00
	Total		<u>\$41,615.20</u>
	Sale of Rams	\$ 500.00	
	Cost per Corp. Books	\$4,701.39	
	Less Deprn.	<u>1,462.84</u>	
	Balance	3,238.55	
	Rams purchased	<u>2,215.00</u>	
	Total	5,453.55	
	Inv. at close 12-31-20		
68 head	@ \$45	<u>3,060.00</u>	<u>2,393.55</u>
	Net Loss		(1,893.55)
	Gross Income		<u>39,721.65</u>

Elmer D. Bryson
SCHEDULE 4-B (cont.)

Explanation of Items—Changed

Deductions:

Labor	\$15,695.16
Board of Labor & Provisions	6,856.72
Int. accrued	1,520.00
Int. and Insurance	2,948.75
Feed	7,594.33
Taxes	1,953.53
Rent	1,180.57
Commission	500.00
Miscl. Repairs	854.21
Auto Expense	2,422.41
Water & Freight	420.25
Incidentals	137.40
Sacks	146.21
Deprn.	1,585.17

Total deductions

43,814.71

Net loss

(4,093.06)

[144]

Sched. D. Net Loss decreased by \$420.00 as follows:

Sale of house & lot to J. K. Fuller	\$3500.00
Acquired 1914 cost	\$4500.00
Deprn. sustained	720.00
Net loss	3780.00

(\$280.00)

Sched. E.

Rent received from Henry Blackman

\$ 80.00

Sched. K. Contributions

Red Cross	\$4.00
Y.W.C.A.	5.00

Total

\$ 9.00

[145]

Treasury Department,
Internal Revenue Service.

Form 845.

Aug., 1921

Name ELMER D. BRYSON

SCHEDULE 5

Year ended 12-31-20

NET INCOME

Net income as disclosed by return.....	\$ 2,586.33
As corrected..... Net loss.....	(4,302.06)
Net (additions—deductions)	6,888.39

Additions:

(a) Loss sale of house disallowed.....	\$ 420.00
() Error in Addn. Sched. H .....	.02
() Error in Subtraction Sched. N.....	.20
()	
()	
()	
()	

Total additions.....	\$ 420.22
----------------------	-----------

Deductions:

() Sched. A revised	\$ 7,308.61
()	
()	
()	
()	

Total deductions.....	\$ 7,308.61
-----------------------	-------------

Net deductions as above.....	6,888.39
------------------------------	----------

[146]

Treasury Department,
Internal Revenue Service.

Form 845 m.

Aug., 1921.

Name ELMER D. BRYSON & WIFE

SCHEDULE 6

COMPUTATION OF TAX

Year—Period ended 12-31-20

Total net income, Schedule 5.....net loss..... (4,302.06)

Less: Exemption

Dividends

Interest on U. S. obligations, etc.

Income subject to Normal Tax..... none

Tax% on.....

Tax% on.....

Tax% on.....

Tax% on.....

Surtax husband's income

Surtax wife's income

Surtax at prior years' rates

Excess Profits Tax, Section 201.....

Excess Profits Tax, Section 209.....

Total Tax

Less tax withheld at source (for 1917 not to
exceed Normal Tax)

Taxes, Section 222, 1918 Act

Total Tax Assessable..... none

Tax previously assessed 7.45

(Overassessment) 7.45

[147]

Treasury Department,
Internal Revenue Service.

Form 845k.

Aug., 1921.

Name ELMER D. BRYSON

SCHEDULE 7

Joint Return form 1040

Year 1921

BLOCK ADJUSTMENTS

Block	Return	Additions	Reductions	Corrected	Wife's Income
2A	\$	\$	\$ 300.00	\$ 300.00	\$.....
5B	(5,444.50)	7,601.19		(13,045.69)	.....
7C		228.75		(228.75)	.....
D					
E					
F					
Total					
11G	(5,444.50)	7,829.94	300.00	(12,974.44)	.....
H					
I					
16J		382.19		382.19	.....
K(a)					
K(b)					
L					
M					
N					
Total	(5,444.50)	8,212.13	300.00	13,356.63	.....

Wife's net income or loss

Husband's net income or loss..... 13,356.63

Elmer D. Bryson

SCHED. 7-A

Explanation of Items—Changed

Item 2.	Int. Received 3d National Bank	\$ 300.00
	Sheep Sales	15,348.94
Item 5.	Wool Sales	5,762.16
	Cottonseed cake sold	608.45

Total sales 21,719.55

Cattle Inv. 1-1-21	\$ 300.00
Sheep Inv. 1-1-21	21,082.00
Rams Inv. 1-1-21	3,060.00
Rams purchased	300.00

Total \$24,742.00

Inventories 12-31-21	
4150 sheep @ 4.78	19,837.00
55 Rams at \$45	2,475.00
Cattle	600.00

Total 22,912.00

Difference 1,830.00

Gross Income 19,889.55

Deductions:

Labor	10,344.00
Supplies & Provisions	2,911.73
Feed purchased	4,555.29
Rent	1,698.27
Accrued Int.	1,641.00
Int. paid	2,820.17
Insurance	77.75
State & County Taxes	3,469.88
Auto Exp. & Traveling	2,619.62
Hardware & Repairs	401.06
Water and Misl.	637.50
Depreciation Ex. F.	1,758.97

Total deductions 32,935.24

Net Loss \$13,045.69

Elmer D. Bryson

SCHED. 7-A (cont.)

Explanation of Items—Changed and Unchanged

Item 7. Sale of Liberty Bonds & War Savings Stamps			
	Sale of Liberty Bonds	\$2,363.25	
	Cost of bonds	2,600.00	
		<hr/>	
	Net loss		\$ 236.75
	War Savings Stamps	\$ 908.00	
	Cost of Stamps	900.00	
		<hr/>	
	Net gain		8.00
			<hr/>
	Net loss Bonds & Stamps		\$ 228.75
Item. 16. Loss sustained as endorser on note for			
	E. L. Davis		\$ 382.19
			[150]

Treasury Department,
Internal Revenue Service.

Form 845.

Aug., 1921

Name ELMER D. BRYSON

SCHEDULE 8

Year ended 12-31-21

NET INCOME

Net income as disclosed by return	Net Loss.....	\$(5,444.50)
As corrected	Net Loss.....	(13,356.63)
Net additions		7,912.13

Additions:

(a)	Adjustment on an Inv. loss.....	\$ 7,601.19
()	Loss Liberty Bonds & W. S. S.	228.75
()	Endorser on note	382.19
()	
()	
()	
()	
	Total additions.....	\$ 8,212.13

Deductions:

()	Int. from 3d Natl. Bank.....	\$ 300.00
()	
()	
()	
()	
	Total deductions.....	\$ 300.00

Net additions as above.....	7,912.13
-----------------------------	----------

[151]

Elmer D. Bryson

SCHED. 8-A

Explanation of Items—Changed

Statutory net loss Article 1601 Reg. 62

Net Loss Sched. 8		\$13,356.63
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Loss taken on note		
--------------------	--	--

Not in business	\$382.19	
-----------------	----------	--

Liberty Bond Int.	68.37	450.56
-------------------	-------	--------

Statutory net loss		(12,906.07)
--------------------	--	-------------

		[152]
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Treasury Department,
Internal Revenue Service.

Form 846.

Aug., 1921.

Name ELMER D. BRYSON & WIFE

EXHIBIT A

Jan. 1, 1920

BALANCE SHEET

Assets	Books	Additions	Reductions	Amended
Liberty Bonds	\$ 2,600.00	\$	\$	\$ 2,600.00
War Sav. Stamps	900.00			900.00
(a) Real Estate	51,365.25	5,209.90		56,575.15
Home	5,000.00			5,000.00
Rams cost	4,701.39			4,701.39
Cattle Inv.	1,925.00			1,925.00
(b) Sheep Inv.	28,720.00	577.00		29,297.00
Pack horses	415.00			415.00
Machinery	300.00			300.00
Pack outfit	8,146.00			8,146.00
Farm Bldgs.	5,801.09			5,801.09
Auto Business	2,200.00			2,200.00
Auto personal	1,300.00			1,300.00
House & lot	4,500.00			4,500.00
Total	17,873.73	5,786.90		123,660.63
Liabilities				
Bank O. D.	487.05			487.05
Notes payable	60,500.00			60,500.00
(c) Dep. Res.	1,680.00	4,426.23	150.00	5,956.23
		5,786.90		
(d) Net Worth	55,206.68	150.00	4,426.23	56,717.35
Total	117,873.73	10,363.13	4,576.23	123,660.63

[153]

Elmer D. Bryson

EXHIBIT A-1

Explanation of Items—Changed

- (a) Real Estate increased by \$5209.90 to agree with the corrected closing balance sheet of the Bryson Robison Corporation, all real estate being taken over by Elmer D. Bryson.
- (b) Inventories increased by \$577.00 to agree with the corrected inventory shown in the report of the corporation as follows:

Old Inventory 1919

1500 Ewes	at \$10.00	\$15,000.00
200 lambs	“ 12.50	2,500.00
700 “	“ 3.30	2,310.00
800 “	“ 4.45	3,560.00
1000 “	“ 5.35	5,350.00

Total	\$28,720.00
-------	-------------

Revised inventory 1919 based on purchases
by the Walla Walla Meat & Cold Storage Co.

1500 ewes	@ \$4.00	\$ 6,000.00
1700 sheep	@ 8.91	15,147.00
1000 lambs	@ 8.15	8,150.00

Total	\$29,297.00
-------	-------------

- (c) Depreciation reserve increased by \$4426.23 amount of depreciation sustained on the assets taken over from the corporation and decreased by \$150.00 excessive reserve set up for gas engine.
- (d) Net worth adjusted by the above changes.

Treasury Department,
Internal Revenue Service.

Form 846.

Aug., 1921.

Name ELMER D. BRYSON & WIFE

EXHIBIT B

Dec. 31, 1920

BALANCE SHEET

Assets	Books	Additions	Reductions	Amended
Liberty Bonds	\$ 2,600.00	\$	\$	\$ 2,600.00
War Sav. Stamps	900.00			900.00
(a) Real Estate	51,685.25	5,209.90		56,895.15
Home	5,356.64			5,356.64
Rams Inv.	3,060.00			3,060.00
Cattle Inv.	300.00			300.00
(b) Sheep Inv.	28,345.00		7,263.00	21,082.00
Pack horses	477.50			477.50
Machinery	507.78			507.78
Pack outfit	8,146.00			8,146.00
Farm Bldgs.	5,801.09			5,801.09
Auto Business	2,200.00			2,200.00
Auto personal	1,300.00			1,300.00
Cabin Tollgate	100.00			100.00
Total	110,779.26	5,209.90	7,263.00	108,726.16
Liabilities				
Bank O. D.	85.53			85.53
Notes payable	53,400.00			53,400.00
Accrued Int.	1,520.00			1,520.00
(c) Dep. Reserve	2,564.78	2,963.39	169.61	5,358.56
		5,209.90	7,263.00	
(d) Net worth	53,208.95	169.61	2,963.39	48,362.07
Total	110,779.26	8,342.90	10,396.00	108,726.16

Elmer D. Bryson

EXHIBIT B-1

Explanation of Items—Changed

- (a) Real Estate increased by \$5209.90, as explained for prior year.
- (b) Inventory of sheep decreased by \$7263, based on purchases by the Walla Walla Meat and Cold Storage Co. on the same basis as prior years inventories of the corporation.

Inventory shown in the con-

structed books	\$28,345.00
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Corrected 4150 head at \$5.08	21,082.00
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Decrease

\$ 7,263.00

- (c) Depreciation reserve increased by \$2963.39 as follows:

Addition to depreciation Res. in the year 1919	\$4,426.23
---	------------

Less depreciation on Rams sold	1,462.84
--------------------------------	----------

Difference

2,963.39

Depreciation reserve decreased by
\$169.00 as follows:

Decreased in the year 1919	\$ 150.00
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Depreciation disallowed 1920	19.61
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Total

\$ 169.61

- (d) Net worth adjusted by the above changes.

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Treasury Department,
Internal Revenue Service.

Form 846.

Aug., 1921.

Name ELMER D. BRYSON & WIFE

EXHIBIT C

Dec. 31, 1921

BALANCE SHEET

Assets	Books	Additions	Reductions	Amended
		76.00		
(a) Real Estate	\$51,685.25	\$ 5,209.90	\$	\$56,971.15
Home	5,356.64			5,356.64
Rams Inv.	2,475.00			2,475.00
Cattle Inv.	600.00			600.00
(b) Sheep Inv.	28,345.00		8,508.00	19,837.00
Pack horses	477.50			477.50
Machinery	1,037.78			1,037.78
Pack outfit	8,146.00			8,146.00
Farm Bldgs.	8,820.98			8,820.98
Auto Business	2,200.00			2,200.00
Auto personal	1,300.00			1,300.00
Cabin Tollgate	100.00			100.00
Total	110,544.15	5,285.90	8,508.00	107,322.05
Liabilities				
Bank O. D.	150.00			150.00
Notes payable	63,214.77			63,214.77
Accrued Int.	3,161.00			3,161.00
(c) Dep. Reserve	4,327.25	2,963.39	173.11	7,117.53
		5,285.90	8,508.00	
(d) Net worth	39,691.13	173.11	2,963.39	33,678.75
Total	110,544.15	8,422.40	11,644.50	107,322.05

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Elmer D. Bryson

EXHIBIT C-1

Explanation of Items—Changed

(a) Real Estate was increased by \$5209.90 as shown for prior year and 76.00 cost of abstract disallowed as expense.

(b) Inventory of sheep decreased by \$8508.00 based on purchases by the Walla Walla Meat and Cold Storage Co., on the same basis as prior years inventories.

Inventory shown in the constructed books	\$23,345.00
Corrected, 4150 head at \$4.78	19,837.00

Difference	\$ 8,508.00
------------	-------------

(c) Depreciation reserve increased by \$2963.39 as shown for prior year, and decreased by \$173.11 as follows:

Decrease in the year 1920	\$ 169.61
Depreciation disallowed 1921	3.50

Total	\$ 173.11
-------	-----------

(d) Net worth adjusted by the above changes.

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Treasury Department
Internal Revenue Service

Form 846A

Aug., 1921

Name ELMER D. BRYSON & WIFE

EXHIBIT D

Analysis of Depreciation Reserve

Date	Item	Debit	Credit	Balance
Jan. 1, 1920	constructed books on assets of corpora- tion taken over not shown on individual books		1,680.00 4,426.23	
	Reserve decreased on Gas Engine	150.00		
Jan. 1, 1920	Corrected Balance			5,956.23
12-31-20	Depreciation allowed Depreciation on Rams sold		1,585.17 1,462.84	
	Depreciation on House sold	720.00		
12-31-20	Corrected balance			5,358.56
12-31-21	Depreciation allowed		1,758.97	7,117.53
				[159]

Treasury Department
 Internal Revenue Service
 Form 846A
 Aug., 1921

Name ELMER D. BRYSON

EXHIBIT E
 Analysis of Net Worth

Date	Item	Debit	Credit	Balance
Jan. 1, 1920	Constructed books		55,206.68	
	Addition to Inventories		577.00	
	Addition to Real Est.		5,209.90	
	Depreciation Reserve decreased on Gas Engine		150.00	
	Depreciation on assets taken over from Corp.	4,426.23		
Jan. 1, 1920	Corrected Balance			56,717.35
12-31-20	Net Loss	4,302.06		
	Liberty Bond Int. Non-Taxable		115.37	
	Personal withdrawals	3,739.38		
	Income Tax a/c Corp.	368.21		
	Gifts	61.00		48,362.07
12-31-21	Net Loss	13,356.63		
	Personal withdrawals	1,387.61		
	Income Tax	7.45		
	Liberty bond Int.		68.37	33,678.75
				[160]

Elmer D. Bryson & Wife

EXHIBIT F

Depreciation

Explanation of Items—Changed

Sheep Sheds &

Farm Bldgs. Rate 4%

Year	Balance	Res. credited	Cost Accumulated Deprn.	1919	Amount Allowed 1920	1921
1920	5801.09	232.04	5801.09	507.29	232.04	232.04
1921	8820.98	352.84	3019.89			120.80
Total	8820.98	584.88	8820.98	507.29	232.04	352.84
	Depreciation Taken				232.04	352.84

Increase (Decrease)

None None

Pack Outfits Rate 10%

1920	8146.00	814.60	8146.00	2414.60	814.60	814.60
1921	8146.00	814.60				
Total	8146.00	1628.20	8146.00	2414.60	814.60	814.60
	Depreciation Taken				814.60	814.60

Increase (Decrease)

None None

Pack Horses Rate 10%

1920	477.50	47.75	477.50	41.50	47.75	47.75
1921	477.50	47.75				
Total	477.50	95.50	477.50	41.50	47.75	47.75
	Depreciation Taken				47.75	47.75

Increase (Decrease)

None None

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Elmer D. Bryson & Wife

EXHIBIT F (cont.)

Depreciation

Explanation of Items—Changed

Year	Balance	Res. credited	Cost	Accumulated Deprn.	1919	Amount Allowed 1920	1921
Machinery Rate 10%							
1919	\$ 300.	\$ 60.	\$ 300.	\$120.	\$ 30.	\$ 30.	\$30.
1920	507.78	70.39	207.78			20.78	20.78
1921	1037.78	107.28	530.00				53.00
Total	1037.78	237.67	1037.78	120.	30.	50.78	103.78
Depreciation Taken					60.	70.39	107.28
Increase (Decrease)					\$ 30.	\$ 19.61	3.50
Automobile Rate 20%							
				6 mos.			
1919	2200.00	440.00	2200.00	220.00	440.00	440.00	440.00
1920	2200.00	440.00					
1921	2200.00	440.00					
Total	2200.00	1320.00	2200.00	220.00	440.00	440.00	440.00
Depreciation Taken					440.00	440.00	440.00
Increase (Decrease)					None	None	None
Dwelling House Rented Rate 4%							
1914 to 1919							
	3000.00	120.00	3000.00	600.00	120.00	Sold	

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Summary			
	1919	1920	1921
Sheep Sheds & Farm Bldgs.		232.04	352.84
Pack Outfits		814.60	814.60
Pack Horses		47.75	47.75
Machinery	30.00	50.78	103.78
Automobile	440.00	440.00	440.00
Dwelling rented	120.00		
Total	590.00	1,585.17	1,758.97
Depreciation taken	620.00	1,604.78	1,762.47
Increase (Decrease)	(30.00)	(19.61)	(3.50)

[163]

FORM FOR ACKNOWLEDGMENT OF
RECEIPT OF REPORT

Instructions:

Do not sign this form unless you are satisfied with the findings of the examining officer. Any protest or objections to his findings should be mailed to INTERNAL REVENUE AGENT IN CHARGE, 807 Fourth Avenue, Seattle, Washington, in triplicate, within 20 days from the date of the letter transmitting copy of report.

If, however, you are in agreement with the findings as stated in the report, please date and sign this form and return same in the enclosed self-addressed envelope at once in order that your case for the period indicated may be closed without delay. The carbon copy may be retained in your files.
No. 7518-W

Place: Walla Walla, Wash.

Date:

To Internal Revenue Agent in Charge,
807 Fourth Avenue,
Seattle, Washington

Receipt is acknowledged of a copy of a report dated Oct. 24, 1924 covering investigation of the Income Tax liability of the undersigned, by Internal Revenue Agent Frank Johnson for the Cal years 1919, 1920 and 1921 a net overassessment of \$7.45.

The undersigned agrees to the findings of the examining officer, and requests that the original of said report be forwarded at once to the Com-

missioner of Internal Revenue, Washington, D. C. for final action.

The undersigned further waives any right of appeal which may be granted under either the Revenue Act of 1921 or the Revenue Act of 1924, and hereby requests the Commissioner of Internal Revenue, Washington, D. C. to immediately close the case for the period stated upon the basis of the said report.

It is understood, however, that the findings of said report are subject to the approval of the Commissioner and that the undersigned is to be notified, before final action, of any material adjustment in said findings.

(Sign here) ELMER D. BRYSON
(Address)

Note: Give full postoffice address.

If executed by a corporation, the full official title of the officer signing for the corporation should be given. [164]

[Title of Court and Cause.]

PRAECIPE FOR RECORD

To the Clerk of the United States Board of Tax Appeals:

You will please prepare, transmit and deliver to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, copies duly certified as correct of the following documents and records in the above entitled cause in connection with the petition for review by the said Circuit Court of Appeals for the Ninth Circuit, heretofore filed by the Commissioner of Internal Revenue:

1. Docket entires of the proceedings before the Board.
2. Pleadings before the Board,
 - (a) Petition, including annexed copy of deficiency letter.
 - (b) Answer.
 - (c) Amendment to answer.
3. Findings of fact, opinions and decisions of the Board, including:
 - (a) Findings and opinion promulgated February 26, 1931.
 - (b) Decision entered February 26, 1931.—
Not of record.
 - (c) Memorandum opinion and Order entered March 28, 1931.
 - (d) Memorandum opinion entered July 20, 1932.
 - (e) Order entered September 22, 1932.
 - (f) Decision entered January 26, 1933.

4. Petition for review, together with proof of service of notice of filing petition for review and of service of a copy of petition for review.

5. Statement of the evidence, as settled and allowed, together with [165] all Exhibits.

6. Orders enlarging time for the preparation of the evidence and for the transmission and delivery of the record.—Not included in record.

7. This praecipe.

(Signed) C. M. CHAREST,

General Counsel,

Bureau of Internal Revenue.

Service of a copy of the within praecipe is hereby admitted this 26 day of June, A. D. 1933.

(Signed) HERBERT C. BRYSON

Attorney for Respondent.

[Endorsed]: United States Board of Tax Appeals.
Filed Jun. 30, 1933. [166]

[Title of Court and Cause.]

CERTIFICATE

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 166, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praeceptum in the appeal as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 8th day of June, 1934.

[Seal]

B. D. GAMBLE

Clerk,

United States Board of Tax Appeals.

[Endorsed]: No. 7519. United States Circuit Court of Appeals for the Ninth Circuit. Guy T. Helvering, as Commissioner of Internal Revenue, Petitioner, vs. Elmer D. Bryson, Respondent. Transcript of the Record. Upon Petition to Review an Order of the United States Board of Tax Appeals.

Filed June 15, 1934.

PAUL P. O'BRIEN,

Clerk of the United States Circuit Court of Appeals
for the Ninth Circuit.

No. 7519

United States
Circuit Court of Appeals
For the Ninth Circuit.

ELMER D. BRYSON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Transcript of the Record

Upon Petition to Review an Order of the
United States Board of Tax Appeals.

United States Board of Tax Appeals.

Docket No. 22,255

DAVID BURNET, Commissioner of Internal
Revenue,

Petitioner,

vs.

ELMER D. BRYSON,

Respondent.

PRAECIPE FOR RECORD.

To the Clerk of the United States Board of Tax
Appeals:

You will please prepare, transmit and deliver to the Clerk of the United States Circuit Court for the Ninth Circuit, copies duly certified as correct of the following documents and records in the above entitled cause in connection with the cross-appeal and petition for review by the said Circuit Court of appeals for the Ninth Circuit, heretofore filed by respondent:

1. All of the record called for by petitioner's praecipe for record.
2. The motion and affidavits in support thereof in behalf of the respondent dated May 8, 1933 and filed in due course of mail thereafter.
3. Respondent's notice of filing petition for review and cross appeal.

4. Respondent's petition for cross appeal, review and assignments of error.

5. This praecipe.

HERBERT C. BRYSON,

Attorney for respondent.

312-3 Drumheller Building,
Walla Walla, Washington.

State of Washington

Walla Walla County—ss.

I, Herbert C. Bryson, sworn, on oath depose and say: I am respondent's counsel, and reside at Walla Walla, Washington; I have this day deposited in the U. S. Post office at Walla Walla, properly stamped, and addressed to General Counsel of the petitioner, Washington, D. C. a true and exact copy of the foregoing praecipe for record in the above entitled cause.

HERBERT C. BRYSON.

Sworn to and subscribed before me June 26, 1933.

J. G. THOMAS

Notary Public for Washington,

(L.S.)

residing at Walla Walla. [1*]

[Endorsed] United States Board of Tax Appeals.
Filed Jun 28, 1933.

[Title of Court and Cause.]

MOTION

Now comes the petitioner, by Herbert C. Bryson, his attorney, and respectfully moves the Board to

*Page numbering appearing at the foot of page of original certified Transcript of Record.

vacate the entry of the final order which was entered here in January 26, 1933, or in the alternative to vacate and re-enter said final order as of April 3, 1933, in order that the right of review of the portion of the final order herein adverse to this petitioner be properly protected. This motion is based upon the records and files in this case before the Board, and affidavits annexed hereto, and the acts of Congress requiring that notice and opportunity to be heard shall be accorded the taxpayer and the commissioner as to all matters and things before the Board. The records of this board and the affidavits annexed must clearly establish that notice of the Board's decision of January 26, 1933, was never afforded petitioner, nor was he apprised thereof, until April 25, 1933, thus depriving the petitioner of inherent and valuable rights without due process of law or any notice or opportunity to be heard.

HERBERT C. BRYSON,

Attorney for Petitioner.

[Endorsed]: United States Board of Tax Appeals.
Filed May 13, 1933. [2]

[Title of Court and Cause.]

AFFIDAVIT

State of Washington

County of Walla Walla—ss.

I, the undersigned, being first duly sworn on oath, depose and say:

That I am registry clerk at the United States post office at Walla Walla, Washington, and in my official capacity as such registry clerk have access to the registry records and files of the post office of Walla Walla, Washington; I have this day been requested to check up the records of this office as to the delivery of a registered letter from the United States Board of Tax Appeals, the request being made by Mr. Herbert C. Bryson, of this city, the registered letter presumably being addressed to said Herbert C. Bryson; our official records disclose that on January 30, 1933, a registered letter, No. 504728, addressed to John F. Watson, Esq., and Herbert C. Bryson, Esq., Walla Walla, Washington, was received by this post office, delivered to and receipted for by Magna Gustafson, stenographer and secretary for Mr. John F. Watson's law firm. This office has no record of delivery to Mr. Herbert C. Bryson whatever.

[Seal]

L. L. ROSEBORO

Subscribed and sworn to before me May 8, 1933.

HERBERT C. BRYSON

Notary Public for Washington. [3]

[Title of Court and Cause.]

AFFIDAVIT

State of Washington

County of Walla Walla—ss.

John F. Watson, being first duly sworn, on oath, deposes and says:

That the above entitled cause was consolidated for trial and the purposes of taking evidence June 2, 1930, with that certain other appeal wherein Lester L. Robison is petitioner, BTA Docket No. 22184. Except for convenience in taking the evidence, the cases were not further consolidated, affiant, as attorney of record for said Robison separately briefing and presenting to the board the case of said Robison wholly independent of petitioner Bryson; petitioner Bryson appeared by Herbert C. Bryson, his attorney, who alone appeared for and represented him; at no time, in no manner, did I appear for or represent Elmer D. Bryson, petitioner, nor have I joined said petitioner's counsel in any brief, motion, application or proceeding before this board; excepting the taking of evidence the cases of the two petitioners have been handled wholly separately, briefed and presented independently of each other, and without collaboration between counsel.

This honorable board, on or about February 26, 1931, promulgated its de- [4] cision discharging petitioner Robison from liability for any of the claimed tax 22 B.T.A. 395. Since receipt of official notice of the order and decision referred to neither affiant nor petitioner Robison have had further to

do before this board with any matter pending before it in connection with claimed liability for income and profit taxes of Bryson-Robison Corporation, nor has affiant nor his client filed any document or pleading before this board since the order referred to.

That on or about January 30, 1933, affiant received, by registered mail from the United States Board of Tax Appeals its notice of final decision in the above entitled cause, dated January 26, 1933; as affiant now recalls the envelope containing said decision was addressed to "Herbert C. Bryson, Esq., and John F. Watson, Esq., Walla Walla, Washington", and the same was received at the United States Post Office at Walla Walla by my stenographer, Magna Gustafson, who delivered the same to me. I assumed that Mr. Bryson had received like copy thereof, and at no time nor at all, prior to the date hereof, have I discussed the matter with either Elmer D. Bryson, or Herbert C. Bryson, his attorney. Because of my belief that Mr. Bryson had undoubtedly received such copy, I in no manner communicated to him the information therein contained, or that a final decision had been made by this board.

JOHN F. WATSON

Subscribed and sworn to before me May 8, 1933.

[Seal]

T. P. GOSE

Notary Public for Washington,
residing at Walla Walla. [5]

[Title of Court and Cause.]

AFFIDAVIT

State of Washington

County of Walla Walla—ss.

Herbert C. Bryson, being sworn says: That he is attorney for the petitioner above named, and has acted as the sole attorney for petitioner throughout the proceedings in this case before the board.

On April 25, 1933, notice of filing petition for review, petition for review and assignments of error, for review by the U. S. Court of Appeals, Ninth Circuit, were served upon affiant at Walla Walla by Frank Johnson, resident Internal Revenue Agent. This was the first official information either the affiant or his client, the petitioner herein, had that this board had rendered final decision in this case. Immediately upon such service, affiant wired Honorable Eugene Black, board member before whom the evidence was taken, requesting copy of the final decision by air mail; without any delay whatever thereafter affiant prepared, caused to be served and filed the petitioner's notice of filing petition for review, and petition for review and assignments of error, as a cross appeal, to be reviewed by the United States Circuit Court of Appeals, Ninth Circuit. The same and all thereof are now matters of record before this court. [6]

This is the second time decisions have been made by this Board, and this affiant has not been apprised thereof until long thereafter, and affiant assumes

that the Board likely thus erroneously presumed to mail notice to affiant by jointly addressing to affiant and John F. Watson, the letters being delivered to Mr. Watson, who at no time informed affiant thereof. On July 30, 1932, affiant filed with this Board petitioner's motion for review of the decision of Mr. Black. Affiant had no information whatever, nor report from the Board, that said motion had been acted upon by the Board until November 10, 1932, when he received from the Commissioner, or the Board notice under Rule 50 that on November 30, 1932, the Board would redetermine tax liability for 1919. On that date affiant wrote the Board inquiring why this step was taken in advance of a decision on the pending motion, and then, for the first time, ascertained from Honorable Eugene Black that the motion had been passed upon adversely on August 4, 1932. I assume that the envelope transmitting the Board's decision of August 4, 1932, had very likely been addressed to both Mr. Watson and myself, was received by Mr. Watson and its contents in no manner disclosed to me, although Mr. Watson in no manner appeared as counsel in the motion for review.

I do not feel that a final disposition of a case under the situation of this one is truly and properly made by the Board by entering a final decision with the clerk, not notifying the one active attorney interested therein of the decision until that attorney accidentally finds out that a decision has been made possibly too late to protect a very vital interest of

his client by appeal which the law gives a litigant before the Board the right to avail himself of. I do not question the good faith of any one in connection with this matter, but I do say that a decision by the Board, according to the records of the Board, January 26, 1933, after disposing of objections and a motion which I alone interposed representing the petitioner in this case; I was not advised of this until April 25, 1933, when the Commissioner appealed to the Circuit Court. There certainly was no occasion to jointly [7] mail notice of the Board's final order to Mr. Watson and affiant jointly, which clearly resulted in no notice whatever to the only counsel of petitioner in this case. Affiant verily believes that the rules of the Board, and Revenue Act of June 2, 1914 creating this Board, 43 Stat. 336 (a), fully contemplate and intend that a litigant before the Board shall have notice and an opportunity to be heard and that the same requires of the Board that "notice and opportunity to be heard upon any proceeding instituted before the Board shall be given the taxpayer and the Commissioner * * *"; that such notice was not afforded the petitioner herein and/or his counsel, and the Board records, the affidavits hereto annexed, and this affidavit clearly show that petitioner was not afforded the notice contemplated by law ere a decision be treated as entered so as to set running the time of the taxpayer for appeal therefrom.

It is now respectfully requested that the Board transmit, along with the full record for review, this

and the subjoined affidavits of John F. Watson and
Postal Registry Clerk, L. L. Roseboro.

HERBERT C. BRYSON.

Sworn to and subscribed before me May 8, 1933.

[Seal]

J. W. THOMAS

Notary Public for Washington,
residing at Walla Walla. [8]

In the United States Circuit Court of Appeals,
Ninth Circuit.

B.T.A. Docket No. 22,255.

DAVID BURNET, Commissioner of Internal
Revenue,

Petitioner,

v.

ELMER D. BRYSON,

Respondent.

PETITION FOR CROSS-APPEAL, REVIEW
AND ASSIGNMENTS OF ERROR.

To the Honorable Judges of the United States
Circuit Court of Appeals for Ninth Circuit:

NOW COMES Elmer D. Bryson, respondent, by
Herbert C. Bryson, his attorney, and respectfully
shows:

I.

The petitioner above named is the duly appointed,
qualified and acting Commissioner of Internal Rev-

enue of the United States. The respondent and cross-appellant is an individual, resident of Walla Walla, Washington, within this Circuit of this honorable court. The income and profits tax returns for the years 1917, 1918, and 1919 were filed with the Collector of Internal Revenue at Tacoma, Washington, which district lies within the Ninth Judicial Circuit.

II.

The Bryson-Robison Corporation was, throughout 1917 and 1918, and until June 4, 1919, a corporation, organized under the laws of Washington, with its place of business at Walla Walla therein. The capital stock in said corporation was owned equally by respondent, Elmer D. Bryson, and Lester L. Robison. On June 4, 1919 Elmer D. Bryson, respondent, purchased of and from said corporation and Lester L. Robison and wife, all of the assets, real and personal and wherever situated, of said corporation. The properties were appropriately conveyed to respondent for a consideration of \$70,000.00, and the payment by respondent of certain outstanding obligations of the [9] corporation. Respondent did not either purchase or acquire the corporate capital stock of Robison, nor did he following June 4, 1919, conduct any business by or in the name of the corporation, on the contrary, from that date forward operated the business as an individual, sole-owner by purchase, thereof.

III.

The petitioner determined a deficiency in income and profit taxes of Bryson-Robinson Corporation for the calendar year of 1917 in the sum of \$2863.42, for the calendar year 1918, \$5741.89, and for the calendar year 1919, \$2973.54. Presuming to act under Sec. 280, Revenue Act of 1926 the petitioner sent respondent and Lester L. Robison by registered mail, a notice of deficiency and proposed assessment against each of them for \$5789.43 as constituting their individual and separate liabilities as transferees of said corporation in the aggregate total of \$11578.85 assessed against such corporation for the said years 1917, 1918 and 1919. Thereafter the respondent filed with the United States Board of Tax Appeals his petition for re-determination of the deficiencies proposed against him in the notice of deficiency, the same being docketed as BTA No. 22255; an identical petition was filed by Lester L. Robison, petitioner in said United States Board of Tax Appeals the same being BTA Docket No. 22184. The two petitions and cases were consolidated. The consolidated cases were heard by the Board of Tax Appeals June 2, 1930. On February 26, 1931, the Board promulgated its interlocutory decision, 22 BTA 395, a second interlocutory decision, unreported, March 28, 1931, a third interlocutory decision unreported, July 20, 1932, a fourth interlocutory decision August 22, 1932, also unreported, a fifth interlocutory decision, unreported on September 22, 1932, and on January 26, 1933, entered its final decision and order of redetermination wherein it ordered and

decided that the respondent was not liable for the deficiencies in the income and profit taxes due from Bryson-Robison Corporation, for the years 1917 and 1918 because his liability was barred by the statute [10] of limitations, but ordering and adjudging the respondent, Elmer D. Bryson, liable as transferee of the assets of said corporation for deficiency due from said corporation for the calendar year 1919 in the of \$2273.54 with interest thereon as provided by law.

The board, in its decision promulgated February 26, 1931, held that Lester L. Robison is not liable as a transferee, predicated decision on the fact that Robison received \$70000.00 cash derived from the assets of the corporation entirely, while respondent received, by purchase, the assets of the corporation from which he obtained the \$70000.00 paid to Robison.

Over objections and exceptions of counsel for this respondent and Lester L. Robison, at the time of the trial on June 2, 1930, the Commissioner was permitted to amend his answer so that he was permitted to seek recovery from each of the stockholders in said corporation, to-wit, Elmer D. Bryson, respondent here, and Lester L. Robison, the full amount of \$11578.85, with accrued penalty and interest, assessed against said Bryson-Robison Corporation, thus permitting, on June 2, 1930, 100 per cent increased assessment of deficiency against each of the said alleged transferees over that demanded of them November 3, 1926 within the time permitted by the revenue act of 1926.

IV.

The respondent is in accord with the decision of the Board of Tax Appeals to the extent of its decision and order that the commissioner is barred by the statute of limitations from recovery from this respondent of income and profit taxes, as a transferee of said corporation, for the years 1917 and 1918. Other than that this respondent requests review of the entire record, each and every decision and order promulgated by the Board touching upon the liability of respondent and/or Lester L. Robison as alleged transferee of said corporation for income and profit taxes claimed from said corporation for 1919. [11]

V.

On October 31, 1932, the Commissioner filed with the Board notice under Rule 50, that this proceeding would be called up for hearing before the Board November 30, 1932, for the purpose of having the Board enter its decision upon the Commissioner's proposed computation and determination of tax for 1919. Detailed objections to the proposed computation were regularly filed with the Board. On January 26, 1933, the Board denied and overruled the objections to the computation and on that date promulgated its decision finding and adjudging the respondent liable as a transferee of the assets of Bryson-Robison Corporation for deficiency due from said corporation for the year 1919 of \$2273.54 with interest as provided by law.

VI.

The record before the Board is clear and undisputed as to the following facts concerning the income and profit tax liability for 1919;

This proceeding involves alleged income and profit tax liability of the respondent solely as a transferee of Bryson-Robison Corporation, and not for any personal or other income of the respondent.

June 4, 1919, respondent acquired by purchase for \$70000.00 all of the assets of Bryson-Robison Corporation, thereafter conducting the business as an individual. The assets were conveyed to respondent by deed and bills of sale executed by the corporation and Lester L. Robison and wife.

The corporation in every manner ceased business June 4, 1919. Its gross and only income for the calendar year 1919 was regularly reported to the Collector of Internal Revenue, Tacoma, Washington, as a closing report for the part year 1919 and the computed tax of \$2.50 was paid and transmitted therewith. The gross income of the corporation was \$2750.00. [12]

The Bryson-Robison Corporation was a sheep farming corporation whose entire income was produced by the sales of wool, sheep and mutton. It had no income from these, or any other sources, except as above specified, for the portion of the calendar year to June 4, 1919, when it ceased business. The remainder of the calendar year 1919 the plant was owned, managed, conducted and operated by respondent as the individual owner thereof. His

income and profit tax report for the calendar year 1919 embraced and included therein the income and profits on the entire plant theretofore owned and operated by said corporation from June 4, 1919, for the remainder of that calendar year. It showed substantial incomes by the respondent personally, and his personal return is not here in controversy.

In 1924 the revenue agent acting for and on behalf of the petitioner audited in complete detail the business of the corporation to June 4, 1919, and the remainder of the calendar year of respondent in the operation of the plant so purchased. The detailed findings and items embraced therein is exhibit No. 7 on file with the Board. The findings, when analyzed, establish our contention as above that the corporation had no taxable income whatever to the date it ceased business, June 4, 1919. The Commissioner, in order to "pull back" into and as corporation business computed the income and profit for the plant itself for the calendar year 1919 and divided the tax liability by days using the gross entire year's income as the basis, and the sole basis, upon which he computed the income and profits tax for the corporation for the part year to June 4, 1919. The Board adopted that basis of computation, charging to the corporation 154/365ths of the gross income of the plant for the entire calendar year, fixing that proportion as the income of the corporation to June 4, 1919, instead of the true fact that the corporation for that year, to the date it quit business, had no income.

VII.

The nature of the controversy on this cross appeal and respondent's re- [13] quest for review gives rise to the following question:

1. Is the respondent a transferee of the assets of Bryson-Robison Corporation within the true intent and meaning of the law with reference thereto as of the date of the transactions of June 4, 1919, when he acquired the plant of said corporation, to an extent which would render him liable for all, or a ratable portion, of the income and profit tax of said corporation should any such be found due?

2. Had the petitioner the legal right to increase the proposed assessment which he proposed November 3, 1926, by 100 per cent against the respondent on June 2, 1930, the date of hearing, long after the expiration of time within which an assessment could be made?

3. If either this respondent or Lester L. Robison be liable for income and profit taxes as alleged transferees of assets of said corporation, are they not equally liable, and the right of recovery, if any, of the petitioner against each of them for an equal one half of the claimed tax?

4. Is the true basis for determining income and profit tax for 1919 of Bryson Robison Corporation the income of said corporation for the part year to the date it ceased business, June 4, 1919, or, is it taxable for income obtained by an individual purchaser of its entire plant from the operation of the plant after the corporation had, in good faith, sold,

conveyed and delivered its entire property and assets to an individual?

5. Was the settlement and adjustment proposed by the Internal Revenue Agent in 1924, exhibit 7 on file with the Board, by the refund to respondent by petitioner of the overpayment therein shown, final and conclusive upon the Commissioner as to claimed income and profit tax liability from said corporation for 1919?

VIII.

The respondent, and cross appellant, desires to obtain a review of the [14] aforementioned decision of the United States Board of Tax Appeals by this Honorable Court.

IX.

The respondent, and cross appellant, says that in the record and proceedings before the United States Board of Tax Appeals and in the decisions and order of redetermination promulgated by the Board, manifest error occurred, upon which he relies to reverse the said decision and order of redetermination so promulgated and entered by the Board, to-wit:

1. The Board erred in permitting the petitioner on June 2, 1930, to increase his proposed additional assessment of 100 per cent, by filing an amended answer at that time seeking recovery of the full amount of the alleged taxes from each of the alleged transferees of assets of Bryson-Robison Corporation, namely, the respondent, Elmer D. Bryson and Lester L. Robison.

2. The Board erred in holding Lester L. Robison on any other or different basis of liability for claimed taxes than the respondent, Elmer D. Bryson.

3. The Board erred in holding that Elmer D. Bryson, respondent, is a transferee of the assets of the Bryson-Robison Corporation, and that he was other than a purchaser thereof for full value from said corporation and Lester L. Robison and wife.

4. The Board erred in finding that the Bryson Robison Corporation owed any income or profit tax at the time it ceased business June 4, 1919.

5. The Board erred in assessing tax liability to Bryson-Robison Corporation for income and profit in no manner earned or received by it, but earned and received solely by its vendee after said corporation ceased business.

6. The Board erred in approving and redetermining tax for 1919 against said corporation on a comparative computation of the portion of year it operated instead of upon the basis of its true and actual income.

7. The Board erred in deciding and ordering that this respondent is liable as transferee of the assets of the Bryson-Robison Corporation for deficiency for the year [15] 1919 in *the of* \$2273.54, together with interest thereon as provided by law, or that he is liable in any other sum whatever.

WHEREFORE the respondent and cross appellant to the end that there be no multiplicity of suits arising from these inter-related issues, petitions that the decision of the Board of Tax Appeals be reviewed

by the United States Circuit Court of Appeals for the Ninth Circuit, as to the issues, matters and things hereinabove set forth and pleaded, that a transcript of the record be prepared in accordance with law, and with the rules of said court, and transmitted to the Clerk of said court for filing, and that appropriate action be taken to the end that the errors herein complained of may be reviewed and corrected by said court, and that the alleged errors complained of by the petitioner be found and adjudged not erroneous and affirmed.

HERBERT C. BRYSON

Attorney for Respondent.

312-13 Drumheller Bldg.

Walla Walla, Washington.

State of Washington,
County of Walla Walla.—ss.

Elmer D. Bryson, being duly sworn, says: That he is the respondent and cross appellant in the foregoing cross appeal and petition for review, and is familiar with the contents thereof; that said petition is true of his own knowledge except as to the matters therein alleged on information and belief, and as to those matters he believes it to be true.

ELMER D. BRYSON

Subscribed and sworn to before me April 28th, 1933.

[Seal]

HERBERT C. BRYSON

Notary Public for Washington

My commission expires January 3, 1937.

[Endorsed]: Filed May 4, 1933. [16]

[Title of Court and Cause.]

NOTICE OF FILING PETITION FOR
REVIEW AND CROSS APPEAL.

To: David Burnet, Commissioner of Internal Revenue, C. M. Charest, General Counsel Bureau of Internal Revenue, Washington, D. C.

You are hereby notified that the respondent above named has filed herewith with the Clerk of the United States Board of Tax Appeals, at Washington, D. C. his cross appeal and petition for review by the United States Circuit Court of Appeals for the Ninth Circuit, of the decision of the Board heretofore rendered in the above entitled case. A copy of the petition for review and cross-appeal and the assignments of error as filed is hereto attached and served upon you.

Dated April 28, 1933.

HERBERT C. BRYSON

Counsel of Record for Elmer D. Bryson,
Respondent.

Personal service of the above and foregoing notice, together with a copy of the petition for review on cross-appeal and assignments of error mentioned therein is hereby accepted and acknowledged this 2nd day of May A. D. 1933.

.....
Commissioner of Internal Revenue
(Sgd) C. M. CHAREST

General Counsel,
Bureau of Internal Revenue.

[Endorsed]: United States Board of Tax Appeals. Filed May 4, 1933. [17]

United States Board of Tax Appeals
Washington

Docket No. 22255

ELMER D. BRYSON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CERTIFICATE.

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 17, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 8th day of June, 1934.

[Seal]

B. D. GAMBLE,

Clerk,

United States Board of Tax Appeals.

[Endorsed]: No. 7519. United States Circuit Court of Appeals for the Ninth Circuit. Elmer D. Bryson, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Upon Petition to Review an Order of the United States Board of Tax Appeals.

Filed July 2, 1934.

PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of Appeals
for the Ninth Circuit.

No. 7519

**In the United States Circuit Court of
Appeals for the Ninth Circuit**

**GUY T. HELVERING, COMMISSIONER OF INTERNAL
REVENUE, PETITIONER**

v.

ELMER D. BRYSON, RESPONDENT

**ON PETITION FOR REVIEW OF DECISION OF THE UNITED
STATES BOARD OF TAX APPEALS**

BRIEF FOR THE PETITIONER

FRANK J. WIDEMAN,
Assistant Attorney General.

**SEWALL KEY,
L. W. POST,**
Special Assistants to the Attorney General.

FILED

JAN 18 1935

PAUL P. GIBBEN,

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**In the United States Circuit Court of
Appeals for the Ninth Circuit**

No. 7519

GUY T. HELVERING, COMMISSIONER OF INTERNAL
Revenue, petitioner

v.

ELMER D. BRYSON, RESPONDENT

*ON PETITION FOR REVIEW OF DECISION OF THE UNITED
STATES BOARD OF TAX APPEALS*

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The only previous opinions in this case are those of the United States Board of Tax Appeals, one of which (R. 23-34) is reported in 22 B. T. A. 395, and the others (R. 35-59) are unreported.

JURISDICTION

This proceeding involves deficiencies in income and profits taxes for the years 1917 and 1918, in the respective amounts of \$2,863.42 and \$5,741.89, and is taken from the decision (order

of redetermination) of the Board of Tax Appeals entered January 26, 1933 (R. 56-59). The case is brought to this Court by petition for review filed April 19, 1933 (R. 59-69), pursuant to the provisions of the Revenue Act of 1926, Sections 1001-1003, c. 27, 44 Stat. 9 as amended by the Revenue Act of 1932, Section 1101, c. 209, 47 Stat. 169.

QUESTION PRESENTED

Whether the liability of respondent, as transferee of the assets of the Bryson-Robison Corporation, for income- and profits-tax deficiencies due from that corporation for 1917 and 1918, is barred by the statute of limitations.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix, *infra*, page 22.

STATEMENT

The facts as found by the Board of Tax Appeals (R. 25-29, 43-44, 47-49) are substantially as follows:

In 1916 the Bryson-Robison Corporation was organized under the laws of the State of Washington, for the purpose of engaging in farming, raising sheep, and operating a sheep ranch. Its stock was divided equally between the respondent, Bryson, and one Robison. Robison was president and Bryson was secretary and treasurer. No formal corporate meetings were held and no

regular set of books or accounts was kept. The corporation engaged in business until June 4, 1919, when Bryson purchased Robison's stock and interest, took possession of the corporation's assets and operated the business thereafter as an individual. The corporation was stricken from the records on July 1, 1921, and was further stricken from the records and dissolved July 1, 1924, for failure to pay state license fees, the last fee having been paid for the fiscal year ended June 30, 1919 (R. 25-26).

The corporation filed its income-tax return for 1917 on March 30, 1918, and filed its income-tax return for 1918 on June 16, 1919 (R. 44).

On February 12, 1923, Mr. Bryson executed a waiver agreeing to an extension of time to one year after date for assessment of 1917 income taxes against the corporation. On January 2, 1924, Mr. Bryson executed an unlimited waiver in respect of 1917 and 1918 income taxes of the corporation. Both of these waivers were signed by him as former secretary of the corporation. The waiver of January 2, 1924 was accompanied by a letter signed by Mr. Bryson's lawyer explaining that the corporation was no longer in existence and that Bryson had authority to sign only as an individual who was formerly secretary (R. 27-29).

The waiver of January 1924 was as follows (R. 28-29) :

INCOME AND PROFITS TAX WAIVER

In pursuance of the provisions of subdivision (d) of Section 250 of the Revenue Act of 1921, Bryson-Robinson Corp., of Walla Walla, Washington, and the Commissioner of Internal Revenue, hereby consent to a determination, assessment, and collection of the amount of income, excess-profits, or war-profits taxes due under any return made by or on behalf of the said Corporation for the years 1917 and 1918 under the Revenue Act of 1921, or under prior income, excess-profits, or war-profits tax Acts, or under Section 38 of the Act entitled "An Act to provide revenue, equalize duties, and encourage the industries of the United States, and for other purposes", approved August 5, 1909, irrespective of any period of limitations.

(Sgnd.) ELMER D. BRYSON,
*Former Secretary of the Bryson-
Robison Corp., Taxpayer,*

(Sgnd.) D. H. BLAIR, c.,
Commissioner.

The accompanying letter was as follows
(R. 47-49):

COMMISSIONER OF INTERNAL REVENUE,

Washington, D. C.

SIR: Re: Your IT:CA:Ms. 2506-WHS-
App.

Elmer D. Bryson has handed me your office letter of the 19th inst. addressed to Bryson-Robison Corporation, in his care, advising that it will be necessary for this corpora-

tion within twenty days from the date of your letter to advise you of its acquiescence in the determination of net income and invested capital as found by the Revenue Agent's report dated October 22, 1923, in order that you may further consider an application for computation of tax under the provisions of Section 210, Revenue Act 1917 and Sections 327-8, Revenue Act 1918.

You have already been informed that this corporation has been entirely out of business since July 1919, and since that date has not owned or possessed any property of any character and the corporation has long since been stricken from the corporate rolls of this state where it was incorporated. It has not functioned in any manner since that date, and being stricken from the corporate rolls naturally the former officers of the corporation cannot legally presume to act for it since it no longer exists.

During the life of the corporation Elmer D. Bryson was secretary of the corporation, but will not presume to assume to act in that capacity after all of these years since its dissolution. The only way he could make a report would be that as that of an individual, who was formerly secretary of a corporation which has been defunct for a period of over four and one-half years, and during which period it has neither functioned nor owned any property.

Your office letter above referred to is being by him referred to Cosper Accounting

Company, who has been looking after this matter and it will probably give your letter such further attention and reply as it deems proper and necessary. We deemed it proper that this status of affairs should now again be called to your attention, as no former officer will assume any authority not vested in him.

Yours very truly,

HERBERT C. BRYSON.

Deficiencies were assessed against the taxpayer corporation on March 21, 1924, for 1917, and on September 1, 1925, for 1918. The sixty-day letters to respondent and Robison as transferees were mailed November 3, 1926. The net value of the assets transferred to Bryson exceeded the amount of the deficiencies (R. 29).

The Board of Tax Appeals held that the waivers were not sufficient to extend the periods for assessment and collection of the 1917 and 1918 taxes against the transferor corporation and that since assessment and collection of the liability of the transferor corporation were barred prior to passage of the Revenue Act of 1926, assessment and collection of the liability of respondent, as transferee, were also barred.

SPECIFICATION OF ERRORS TO BE URGED

The Board of Tax Appeals erred:

1. In holding that assessment and collection of income and profits taxes due from Bryson-Robi-

son Corporation, against respondent as a transferee of the property of that corporation, was barred by the statute of limitations.

2. In holding that the waivers executed by the transferee of the assets of the original taxpayer, purporting to extend the time of assessment and collection against the original taxpayer, were ineffective to extend the statute of limitations either as to the original taxpayer or as to the transferee.

3. In failing to hold that the waiver of January 2, 1924, was executed for and on behalf of the Bryson-Robison Corporation and was binding upon it as well as upon respondent individually.

4. In failing to find that by reason of his execution of the waiver of January 2, 1924, respondent secured a postponement to a time beyond the period of limitation, except as extended by the waiver, of the assessment and collection of additional income and profits taxes due from Bryson-Robison Corporation for the years 1917 and 1918.

5. In failing to hold that respondent was estopped to deny the validity of the waiver.

SUMMARY OF ARGUMENT

I. The Board of Tax Appeals erred in holding that the waiver of January 1924 did not bind the corporation, because (1) the corporation was still in existence although it was inactive at the time and its name had been stricken from the records of the Secretary of State of the State of Wash-

ington; (2) the waiver recites that Bryson-Robinson Corporation consents to the extension; (3) the waiver is signed by respondent as former secretary of the corporation; (4) respondent was then the sole stockholder of the corporation and the only person interested in it; (5) subsequent to dissolution, respondent would have been charged with collecting the assets of the corporation and discharging its obligations; and (6) even if the corporation had been dissolved, the execution of the waiver by respondent would have been clearly sufficient to extend the time for assessment of corporate taxes.

II. In any event, respondent as transferee was clearly bound by the waiver, and under *Helvering v. Newport Co.*, 291 U. S. 485, it is immaterial whether or not the statute of limitations had run against assessment of the corporation, for it is undisputed that assessment against respondent as transferee in November 1926 was made within the extended period for assessment provided by the waiver.

III. Apart from the technical aspects of this case, respondent was benefited by execution of the waiver and by signing the same he estopped himself to question its validity.

I

ARGUMENT

The waivers of February 1923 and January 1924 were clearly sufficient to extend the periods for assessment of 1917 and 1918 taxes against the Bryson-Robison Corporation; and such taxes were duly assessed in March 1924 and September 1925 so that assessment against respondent as transferee in November 1926 was timely and entirely in order under the provisions of section 280 of the Revenue Act of 1926

The waiver of February 1923 was a one-year waiver, purporting to extend to February 12, 1924, the period for assessment and collection of 1917 taxes. The waiver of January 1924 was an unlimited waiver with respect to 1917 and 1918 taxes. Without any waiver, the statute of limitations would have run against 1917 taxes on March 30, 1923 (five years after filing of the return) and against 1918 taxes on June 16, 1924 (five years after filing of the return). See Revenue Act of 1921, Sec. 250 (d), and Revenue Act of 1924, Sec. 277 (a) (2), Appendix, *infra*. As it is settled that a waiver is effective when executed after the running of the statute (*McDonnell v. United States*, 268 U. S. 420), it is only necessary to consider whether the waiver of January 2, 1924, was sufficient to extend the periods for assessment against the corporation of 1917 and 1918 taxes so as to make timely the assessments of March 1924 and September 1925. The Board of Tax Appeals decided this question adversely to the Commissioner on the ground that the waiver, when read in the light of a letter which accompanied it, showed

clearly that it was not executed for the corporation, but merely by respondent as an individual. The waiver and letter are hereinbefore set forth in full (pp. 4, 5, and 6).

Mr. Elmer D. Bryson, respondent herein, was on January 2, 1924, the sole stockholder of the corporation and its former secretary and treasurer. There was no other person who had any interest in it. The statement in the letter [written by respondent's lawyer] to the effect that the corporation was no longer in existence was contrary to the law of the State of Washington. The certificate of the Secretary of State of the State of Washington (R. 46) recites that the corporation was stricken from the records on July 1, 1921, for failure to pay taxes, and that the corporation was further stricken from the records and dissolved July 1, 1924; also that the corporation has had no legal existence since July 1, 1921, pursuant to Chapter 140, Laws of 1907. Upon the basis of such recitations in the Secretary of State's certificate, the Board of Tax Appeals concluded that the date of dissolution was July 1, 1921 (R. 46).

Examination of the pertinent Washington statutes shows the conclusion of the Board to be plainly erroneous as a matter of law. These statutes are contained in (1) Laws of 1907, Chapter 140, Sec. 7; (2) Laws of Extraordinary Session, 1909, Chapter 19; (3) Laws of 1911, Chapter 41; and (4) Laws of 1923, Chapter 144, Secs. 5 and 6. These statutes must be read together to obtain the intent of the

legislature with respect to the situation in the instant case. Section 5 of Chapter 144 of the Laws of 1923 provided that any corporation whose name had been stricken from the records of the Secretary of State for failure to pay license fees for two years might apply for reinstatement at any time within three years after its name had been stricken from the records.

Section 4 of Chapter 19 of the Laws of Extraordinary Session, 1909, provided that if, during the period named within which a corporation might make application for reinstatement, such corporation should not make such application, the corporation should be dissolved and the trustees should hold the title to its property for the benefit of stockholders and creditors. Section 5 of Chapter 144 of the Laws of 1923 further provided that any corporation stricken from the records and dissolved might thereafter hold a meeting of stockholders, in the same manner as provided during its corporate existence, and pass such resolutions as might be necessary to close out its affairs and wind up its business. Section 5 of Chapter 19 of the Laws of Extraordinary Session, 1909, provided that the name of no corporation stricken from the records should be adopted by another corporation until the expiration of the time within which application for reinstatement might be made.

Those statutory provisions (other than the ones adopted in 1923) were considered in the case of

State ex rel. Preston Mill Co. v. Howell, 67 Wash. 377, 121 Pac. 861. That case involved an application for a writ of mandamus to the Secretary of State of the State of Washington, directing him to accept fees from relator corporation and issue a license to it. In granting the writ, the court said (pp. 381-382):

So that the law, as it now reads, provides that a corporation failing to pay its annual license fees for two years shall be stricken from the records of the office of the secretary of state; that every corporation so stricken may apply at any time thereafter for reinstatement, and when so applying shall be reinstated upon payment of all license fees and penalties then due, together with an additional penalty of \$100. It will be noted that § 3715d, providing for the dissolution of the corporation for failing to apply within the time in which application might be made for reinstatement, which time was six months as fixed in the act of 1909, has now no force, since the act of 1911 changed the time in which such application might be made from six months to "any time after its name had been stricken from the records"; and, since the dissolution was to take effect at the expiration of the time fixed in which application for reinstatement might be made, and that time is now, under the amendment of 1911, any time after the striking of the name, there is now no time fixed for such dissolution. Section 3715a, as

amended by the act of 1911, reads, "any corporation stricken from the records and dissolved as provided in this chapter", may hold meetings and pass resolutions necessary to close out its affairs and such resolution of such "stricken and dissolved corporation" is validated and approved.

There is no provision, however, in this chapter for the dissolution of such corporation, as to how or when it shall take place; the only penalty to the offending corporation provided for in the act being the striking of its name from the official records of the secretary of state. The framers of this act evidently had in mind the provisions of § 3715d, which made provision for dissolution under the act of 1909. But they failed to fix a time in which the provisions of that section could become operative. The result is there is now no time in which this section, the only one containing any provision for the dissolution of corporations for failure to pay license fees, can become operative. When, therefore, relator applied to the secretary of state to accept its license fee, he should have done so, as it had made full compliance with the law, and within the time provided by the law in force at the time the application was made.

Subsequent to the foregoing decision, the law was amended so as to provide for a period of three years within which a corporation might apply for reinstatement as above set forth (Laws of 1923, c.

144, Sec. 5, *supra*), but the principles laid down in that decision were not otherwise affected.

See also *Patterson v. Ford*, 167 Wash. 121, 8 Pac. (2d) 1006; *Moore v. Los Lugos Gold Mines*, 172 Wash. 570, 21 Pac. (2d) 253.

Applying to the instant case the laws as above set forth, it is clear that the Bryson-Robison Corporation was not dissolved on January 2, 1924, the date of the waiver. The corporation's name was stricken from the records of the Secretary of State on July 1, 1921, but the period for application for reinstatement was of indefinite duration under Section 1 of Chapter 41 of the Laws of 1911 and the three-year period prescribed by the Laws of 1923, *supra*, did not expire until July 1, 1924; so that until that date the corporation continued to exist, having the right to apply for reinstatement and having the exclusive right to its corporate name. Respondent Bryson was the sole stockholder, the sole remaining officer and director (trustee) and the transferee of the corporation's business and assets.

Under such circumstances, the conclusion of the Board of Tax Appeals that Bryson had no authority to act for the corporation in signing the waiver and that he did not purport to do so is manifestly unsound. The waiver recited that the corporation and the Commissioner agreed to an extension of time for assessment and it was signed by Bryson as former secretary of the corporation. While it is true that the accompanying letter stated that

the corporation was dissolved and that Bryson was without authority to act for it, such statement was merely an erroneous conclusion as to the law for the reasons above stated.

In the case of *California Iron Yards Co. v. Commissioner*, 47 F. (2d) 514 (C. C. A. 9th), this Court decided practically the same question as here involved. That case involved the validity of a waiver executed in behalf of a California corporation suspended for nonpayment of license tax. The taxpayer contended that it was prohibited by the state law from making the waiver in question. In holding the waiver valid, this Court said (p. 516):

Moreover, if we concede that the corporation was prohibited by the terms of the state statute from making the waiver in question, such state statute would not control the rights of the corporation or of the government, for the authority to make the waiver in question is not derived from the state of California, but is derived from the United States, and, so long as the corporation retains its status as a taxpayer, it is authorized by the federal government to make such waiver, and the inhibition of the state statute against such action is unavailing. * * *

See also *Angelus Building & Investment Co. v. Commissioner*, 57 F. (2d) 130, 132 (C. C. A. 9th), certiorari denied, 286 U. S. 562.

However, we submit that even if the corporation in the instant case had been dissolved prior to

execution of the waiver, Bryson would still have had power to negotiate with the Government in respect of its income-tax liability. He was the sole remaining stockholder and would have been empowered under Section 5 of Chapter 144 of the Laws of 1923, *supra*, to close out its affairs and wind up its business. He was also the sole remaining director or trustee and under Section 4 of Chapter 19 of the Laws of Extraordinary Session, 1909, he would have been vested with title to the corporate property for the benefit of its stockholders and creditors. See also *Washington Laws of 1866*, p. 64, Sec. 23, which provides that the trustees at time of dissolution of a corporation shall have full power to sue for debts and property of the corporation, by the name of the trustees of the corporation, collect and pay the outstanding debts, settle all its affairs, and divide among the stockholders the money and other property remaining after payment of debts and expenses.

In view of such broad powers, it is perfectly clear that Bryson would have had authority to settle the taxes of the corporation even had it been dissolved and in connection therewith he would clearly have had authority to sign the waiver in question. His action would certainly have been effectual to extend the time for assessment of corporate taxes. Cf. *Soderberg v. McRae*, 70 Wash. 235, 126 Pac. 538; *Helvering v. South Penn Oil Co.*, 68 F. (2d) 420 (App. D. C.).

To summarize, it seems clear that the waiver of January 1924, bound the corporation, because (1) the corporation was still in existence although it was inactive at the time and its name had been stricken from the records of the Secretary of State; (2) the waiver recites that Bryson-Robison Corporation consents to the extension; (3) the waiver is signed by respondent as former secretary of the corporation; (4) respondent was then the sole stockholder of and the only person interested in the corporation; (5) subsequent to dissolution, respondent would have been charged with collecting the assets of the corporation and discharging its obligations; and (6) even if the corporation had been dissolved, the execution of the waiver by respondent was clearly sufficient to extend the time for assessment of corporate taxes.

II

Assuming that the Board of Tax Appeals correctly held that the execution of the waiver by respondent was only binding upon him individually, it is immaterial whether or not the time was extended to permit action against the corporation

The Board of Tax Appeals held that the waiver of January 2, 1924, was executed by respondent individually as transferee of the assets of the original taxpayer, but that it was ineffective to extend the statute of limitations as to the original taxpayer; that assessment and collection of 1917 and 1918 taxes against the corporation were barred

prior to adoption of the Revenue Act of 1926 and hence assessment and collection of the liability of respondent as transferee were also barred. The authorities relied on by the Board included *Newport Co. v. Commissioner*, 22 B. T. A. 833. The decision in that case was affirmed upon review by the Circuit Court of Appeals for the Seventh Circuit (65 F. (2d) 925); but the Supreme Court of the United States granted a writ of certiorari upon petition by the Government (290 U. S. 620), and reversed the judgment of the Court of Appeals. *Helvering v. Newport Co.*, 291 U. S. 485.

In that case the facts were that the Chemical Works, a Maine corporation, after it had filed its tax return for 1917, transferred all its assets to a Delaware corporation, which, as consideration for the transfer, issued its stock to the stockholders of the transferor and assumed all liabilities of the transferor. The Chemical Works was dissolved in 1920. The period of limitation for the assessment and collection of the 1917 taxes expired in April 1923. The question was whether this period was extended by waiver so as to include a deficiency assessment made in March 1927. The Delaware corporation, transferee and taxpayer in the proceedings under review, contended that a waiver of November 6, 1926, executed by it, was ineffective because the statute had run in favor of the original taxpayer. The Court held that the waiver extended the time for assessment against the transferee regardless of the fact that

assessment against the original taxpayer may have been barred prior to the Revenue Act of 1926.

Assuming for argument that the waiver of January 2, 1924, was executed by respondent individually and not as authorized agent for the Bryson-Robison Corporation, the *Newport Co. case* is indistinguishable from the instant case. In the *Newport Co. case* it was held immaterial that the statute of limitations barred the Government from proceeding against the original taxpayer and the assessment in March 1927, against the transferee was upheld. In the instant case, it is accordingly not material whether the waiver of January 1924, extended the Government's time to proceed against the original taxpayer; and since the respondent contended and the Board of Tax Appeals held that the waiver was signed by him as an individual, there can be no question but that the assessment made against him in November 1926, was timely.

See also *Kieckhefer v. United States* (C. Cls.), decided Nov. 5, 1934, found in 343-A C. C. H., par. 9504; *Breene v. United States* (C. Cls.), decided Nov. 5, 1934, found in 343-A C. C. H., par. 9503; *Lucas v. Hunt*, 45 F. (2d) 781 (C. C. A. 5th); *Helvering v. South Penn Oil Co.*, *supra*; *Pacific Coast Steel Co. v. McLaughlin*, 61 F. (2d) 73 (C. C. A. 9th), affirmed 288 U. S. 426; *Commissioner v. Wolf Co.*, 69 F. (2d) 1001 (C. C. A. 3d); *Wonder Bakeries Co. v. United States*, 6 Fed. Supp. 228 (C. Cls.).

III

Apart from technical considerations, the purpose of the waiver was to permit consideration of taxpayer's claim for special assessment; the extension of time was for the benefit of respondent as transferee and real party in interest, and it would be most inequitable to hold that the waiver was invalid and that assessment was barred by the statute of limitations

In view of the fact that the extensions of time for assessment were necessitated by the respondent's claim for special assessment of income and profits taxes of the corporation for 1917 and 1918, under the provisions of Section 210, Revenue Act of 1917, and Sections 327 and 328 of the Revenue Act of 1918; and in view of the additional facts that by reason of executing the waivers, respondent secured consideration of the claims for abatement of the additional income and profits taxes assessed against the corporation for the year 1917, and secured an allowance of the claims to the extent of \$3,033.44, respondent should not be permitted to deny the validity and efficacy of the waivers. Except for the waivers, the Commissioner would have made the assessments within the original periods.

Our view is amply supported by the case of *Lucas v. Hunt, supra*. In that case the question was whether an assessment for 1919 taxes made against Hunt as transferee of the assets of a taxpayer corporation, was barred by the statute of limitations. The corporation was dissolved in 1921 under a statute providing for continuance of

existence and management by liquidators for three years. Hunt was president of the corporation and became a liquidator. In 1924, more than three years after dissolution of the corporation, he executed a tax waiver in its name. The defense made the contention that the waiver was invalid because executed after expiration of the three year period. The court held that Hunt by signing the waiver estopped himself to question its validity, with the result that he was bound to respond to the assessment to the extent of funds in his hands which belonged to the dissolved corporation taxpayer.

CONCLUSION

The decision of the Board of Tax Appeals should be reversed to the extent that it holds that respondent is not liable for any deficiency of the Bryson-Robison Corporation for 1917 and 1918.

Respectfully submitted.

FRANK J. WIDEMAN,
Assistant Attorney General.
SEWALL KEY,
L. W. POST,
*Special Assistants to the
Attorney General.*

JANUARY 1935.

APPENDIX

Revenue Act of 1926, c. 27, 44 Stat. 9:

SEC. 280. (a) The amounts of the following liabilities shall, except as hereinafter in this section provided, be assessed, collected, and paid in the same manner and subject to the same provisions and limitations as in the case of a deficiency in a tax imposed by this title (including the provisions in case of delinquency in payment after notice and demand, the provisions authorizing distraint and proceedings in court for collection, and the provisions prohibiting claims and suits for refunds):

(1) The liability, at law or in equity, of a transferee of property of a taxpayer, in respect of the tax (including interest, additional amounts, and additions to the tax provided by law) imposed upon the taxpayer by this title or by any prior income, excess-profits, or war-profits tax Act.

* * * * *

(b) The period of limitation for assessment of any such liability of a transferee or fiduciary shall be as follows:

(1) Within one year after the expiration of the period of limitation for assessment against the taxpayer, or

(2) If the period of limitation for assessment against the taxpayer expired before the enactment of this Act but assessment against the taxpayer was made within such

period, then within six years after the making of such assessment against the taxpayer, but in no case later than one year after the enactment of this Act. (U. S. C. App., Title 26, Sec. 1069.)

Revenue Act of 1921, c. 136, 42 Stat. 227:

SEC. 250. (d) The amount of income, excess-profits, or war-profits taxes due under any return made under this Act for the taxable year 1921 or succeeding taxable years shall be determined and assessed by the Commissioner within four years after the return was filed, and the amount of any such taxes due under any return made under this Act for prior taxable years or under prior income, excess-profits, or war-profits tax Acts, or under section 38 of the Act entitled "An Act to provide revenue, equalize duties, and encourage the industries of the United States, and for other purposes", approved August 5, 1909, shall be determined and assessed within five years after the return was filed, unless both the Commissioner and the taxpayer consent in writing to a later determination, assessment, and collection of the tax; * * *

Revenue Act of 1924, c. 234, 43 Stat. 253:

SEC. 277. (a) (2) The amount of income, excessive-profits, and war-profits taxes imposed by the Act entitled "An Act to provide revenue, equalize duties, and encourage the industries of the United States, and for other purposes", approved August 5, 1909, the Act entitled "An Act to reduce tariff duties and to provide revenue for the Government, and for other purposes", approved October 3, 1913, the Revenue Act of 1916, the Revenue Act of 1917, the Revenue Act of 1918, and by any such Act as amended,

shall be assessed within five years after the return was filed, and no proceeding in court for the collection of such taxes shall be begun after the expiration of such period (U. S. C. Title 26, Sec. 1057).

Treasury Regulations 69, promulgated under the Revenue Act of 1926:

ART. 1291. *Claims in cases of transferred assets.*—The amount for which a transferee of the property of a taxpayer is liable, at law or in equity, and the amount of the personal liability of a fiduciary under section 3467 of the Revised Statutes, in respect of any income or profits tax imposed by Title II of the Revenue Act of 1926, or by prior Acts, whether shown on the return of the taxpayer or determined as a deficiency in the tax, shall be assessed against such transferee or such fiduciary, as the case may be, and collected and paid in the same manner and subject to the same provisions and limitations as in the case of a deficiency imposed by Title II of the Revenue Act of 1926, except as hereinafter provided. The provisions relating to delinquency in payment after notice and demand and the amount of interest attaching because of such delinquency, the authorization of distraint and proceedings in court for collection, the prohibition of claims for abatement and claims and suits for refund, the filing of a petition with the Board of Tax Appeals, and the filing of a petition for review of the Board's decision, are included in the sections and articles relating to deficiencies in tax imposed by Title II.

The term "transferee" as used in this article includes an heir, legatee, devisee, distributee of an estate of a deceased person,

the shareholder of a dissolved corporation, the assignee or donee of an insolvent person, the successor of a corporation, a party to a reorganization as defined in section 203, and all other classes of distributees.

The period of limitation for assessment of the liability of a transferee or of a fiduciary, referred to in the first paragraph of this article, is as follows:

(1) Within one year after the expiration of the period of limitation for assessment against the taxpayer (see sections 277, 278, and 283 (1), and articles 1271 and 1272); or

(2) If the period of limitation for assessment against the taxpayer expired before the enactment of the Revenue Act of 1926, but assessment against the taxpayer was made within such period, then within six years after the making of such assessment against the taxpayer, but in no case later than one year after the enactment of the Revenue Act of 1926.

(3) If a court proceeding against the taxpayer for the collection of the tax has been begun within the period of limitation for the bringing of such proceeding, then within one year after the return of execution in such proceeding.

For the purpose of determining the period of limitation for assessment against a transferee or a fiduciary, if the taxpayer is deceased, or, in the case of a corporation, has terminated its existence, the period of limitation for assessment against the taxpayer shall be the period that would be in effect had the death or termination of existence not occurred.

If a notice of the liability of a transferee or the liability of a fiduciary has been mailed to such transferee or to such fidu-

ciary under the provisions of section 274 (a) (see Article 1232), then the running of the statute of limitations shall be suspended for the period during which the Commissioner is prohibited from making the assessment, and for 60 days thereafter.

The provisions of section 280 do not apply in any suit or proceeding for the enforcement of the liability of a transferee, or the liability of a fiduciary under section 3467 of the Revised Statutes, which was pending at the time of the enactment of the Revenue Act of 1926.

6

United States
Circuit Court of Appeals
For the Ninth Circuit.

EDMUND J. LORD,

Appellant.

vs.

TERRITORY OF HAWAII,

Appellee.

Transcript of Record

Upon Appeal from the Supreme Court of the
Territory of Hawaii.

FILED

SEP 21 1934

PAUL F. O'BRIEN,
CLERK

No. 7543

United States
Circuit Court of Appeals
For the Ninth Circuit.

EDMUND J. LORD,

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vs.

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Transcript of Record

Upon Appeal from the Supreme Court of the
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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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In the Supreme Court of the Territory of Hawaii.

October Term, 1933.

No. 2052

In the Matter of the Income Tax Appeal
of

EDMUND J. LORD

for the year ending December 31, 1930,
First Taxation Division.

APPEAL FROM TERRITORIAL BOARD OF
EQUALIZATION.

AMENDED RETURN

Territory of Hawaii
First Taxation Division, District of Honolulu

INDIVIDUAL INCOME TAX RETURN
For the Twelve Months Preceding January 1,
1931

Form B18

Ext. No.

Date filed

6/18/31

(Sgd.) H. GLASS

filed by (Sgd.) H. W. Camp

Notice of Proposed Change

Identified.....

Jun. 29, 1931

Reported

(Form B9b-409)

Name Edmund J. Lord

Nationality Age 62

Residence c/o Hawaiian Trust Co. Ltd.

Street and number)

Honolulu

Occupation or Profession

(Kind of Business)

By whom employed

(Name of Employer)

Location of Business

(Street and number)

Telephone No..... P. O. Box No.....

Were you married and living with husband or wife on December 31, 1930? no

If not, what was your status on December 31, 1930?.....

If married, give full name of husband or wife.....

How many dependent persons, other than husband or wife, under 18 years of age, or incapable of self-support because mentally or physically defective, were receiving their chief support from you on December 31, 1930? two

State relationship and age of such dependents

mother and daughter

Is this a joint return of husband and wife?.....

If not, state exemption claimed by husband or wife \$.....

Did you file a return last year? yes

At which office? Honolulu

INCOME

1. Salaries, Wages, Commissions, etc.
(State source from which derived)
(a) \$.....
(b)
2. Gross Income from Business or Profession
- 2a. Merchandise Withdrawals from Business
3. Interest on Bank Deposits, Notes, Mortgages,
Corporation Bonds, Government Bonds
(Foreign or Mainland Municipal Public
Utility), etc. 9,969.99
4. Dividends from Corporations not subject to
Territorial Income Tax:
(List name of Corporation)
.....
5. Net Profit from sale of Real Estate, Stocks,
Bonds, etc. (From Schedule B)
6. Gross Rentals derived from sources within
the Territory
7. Income from Partnerships, Fiduciaries, etc.
(Explain in Schedule D):
(State name and address of partnership, etc.)
8. Exempt Income (Deduct in Item 15 below)
- (a) Dividends from Corporations subject to
Territorial Income Tax:
(List name of Corporation) \$406,569.98 see schedule
Pioneer Mill Co. \$580.
Maui Agri. Co. \$1308. E. J. Lord Ltd 408,457.98

(b) Interest on United States, Territorial or Local Government Bonds	2,901.67
(c) Personal Property acquired by Gift or Inheritance (Explain) :	
.....	
9. Other Income (State Nature of Income)	
10. Total Income in Items 1 to 9	
(Carry to Item 18 at Top)	<u>\$421,329.64</u>

DEDUCTIONS

11. Interest paid (Except on indebtedness incurred outside of Territory) :	
(Itemize)	
(a)	1,420.43
(b)	
12. Taxes paid (Except on Property located outside of Territory) :	
(a) Property Taxes (Not including Frontage or Improvement Taxes)	2,790.64
(b) Territorial Income Taxes	
(c) Federal Income Taxes	11,471.17
(d) Other Taxes (Including Licenses—Explain) :	
Auto tax \$86. — War Tax on club dues \$15.45	101.45
13. Expenses in connection with Item 2 above (From Schedule A)	
14. Expenses in connection with Item 6 above (From schedule C)	
15. Exempt Income (Listed in Item 8 above).....	411,359.65
16. Other Deductions authorized by law (Explain) Commission on collection of income.....	1,131.88
.....	
17. Total Deductions in Items 11 to 16 (Carry to Item 19 at Top)	<u>\$428,275.22</u>

COMPUTATION OF TAX

(Do Not Use)

18. Total Income	\$421,329.64	\$421,329.64
19. Deductions	428,275.22	21,705.24
deficit*		
20. Net Income	6,945.58*	319,624.40
21. Exemption	1,400.00	1,400.00

22. Taxable Income	none	318,224.40
23. Tax	\$ none	\$ 18,686.22
<hr/>		<hr/>
1st Payment		9,343.11
(Delinquent after June 20)		
2nd Payment		9,343.11
(Delinquent after Nov. 15)		

*Denotes red letters and figures.

AFFIDAVIT

I swear (or affirm) that this return has been examined by me and, to the best of my knowledge and belief, is a true and complete return made in good faith.

HAWAIIAN TRUST CO., LTD.

By (Sgd.) H. W. CAMP

Signature of Taxpayer or Agent.

Asst. Secretary.

120 S. King St. Honolulu

Official Capacity and Address of Agent.

Subscribed and sworn before me this 18th day of June, A. D. 1931.

(Notarial Seal)

(Sgd.) H. J. EVENSEN

Deputy Assessor or Notary Public.

Notary Public First Judicial Circuit,

Territory of Hawaii.

SCHEDULE A—EXPENSES OF BUSINESS OR PROFESSION

Cost of Goods Sold:

1. Labor	\$.....
2. Materials and Supplies	
3. Merchandise bought for Sale	
4. Other Costs (List principal items)	
5. Plus Inventory at first of year	
6. Total (Lines 1 to 5 inclusive)	\$.....
7. Less Inventory at end of year	
8. Net Cost of Goods Sold	\$.....

State amount of salary, or its
equivalent, paid to self and
included in Line 9 hereof

\$.....

Other Deductions:

9. Salaries and Wages\$.....
(Not reported in Line 1 hereof)
10. Rent on Business Property
(Where taxpayer has no equity)
11. Insurance on Business Property
12. Depreciation on Business Property.....
(Actually in use)
13. Repairs to Business Property
(Explain below)
14. Bad Debts (Explain below)
15. Other expenses
(List principal items)
16. Total (Lines 9 to 15 inclusive).....\$.....
17. Total Deductions (Line 8 plus Line 16)
(Enter as Item 13)\$.....

Explanation of deductions claimed
(Lines 4, 13, 14 and 15)

.....

.....

.....

State estimated life of property and how depreciation
is arrived at (Line 12)

.....

SCHEDULE B—PROFIT FROM REDEMPTION OF REAL ESTATE, STOCKS, BONDS, ETC.

Kind of Property	Date Acquired	Date Redeemed	Redemption Price	Commis-sions	Cost Price	REAL ESTATE			Net Profit (Enter as Item 5)
						Value 5 Years Prior to Sale	Subsequent Improvements	Total	
600 shs	1926	1930	\$	\$	\$60,000.00	\$	\$	\$	none

E. J. Lord Ltd.

State how 5-year value is determined

SCHEDULE C—EXPENSES OF RENTED PROPERTY

Kind of Property	Commis-sions	Deprecia-tion	Repairs	Insurance	Water, Light, Etc.	Other Expenses	Total (Enter as Item 14)
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State estimated life of property and how depreciation is arrived at

Explain nature of repairs

The New Freedom Press
Com. on Pub. Accy. Form B22.

CORRECTED.

Territory of Hawaii

First Taxation Division Honolulu, T. H. June 19, 1931.

E. J. Lord

c/o Hawaiian Trust Co., Ltd. Honolulu, T. H.

NOTICE OF PROPOSED CHANGE IN ASSESSMENT ON INCOME TAX RETURN

Please be advised that certain items in your income tax return for this year are not in conformity with the law. The following summary shows the amounts returned by you and the corrected amounts as changed by the Assessor.

	AS RETURNED	AS CHANGED
Gross Income	\$527,598.20	\$421,329.64
Deductions	534,543.78	21,705.24
Exemptions	1,400.00	1,400.00
Net Taxable Income	None.	398,224.40
Tax		18,686.22

Corrections are due to Sale of Stock as per schedule submitted.

Unless you can satisfy the Assessor that the figures returned by you are correct, the amended figures will stand as proposed herein.

(Sgd.) CHAS. CHING QUON

Dep. Assessor.

Delivered by H. Glass to Mr. Carter Galt.

6/19/31 (Sgd.) H. GLASS

Territory of Hawaii

9

Received
6/18/31
(s) H. Glass

June 17, 1931

E. J. LORD

1930 Territorial Income Tax

Schedule showing basis of Income Tax Assessor's figure and adjustment thereto to agree with amended return.

Date of Payment		Assessor's Figure
	Proceeds from redemption of 600 shs E. J. Lord Ltd	<u>\$476,074.00</u>
Feb 15 1930	Notes and Bonds \$249,000.00	
	Cash 1,000.00	
Jul 16 1930	Bonds, St. Louis Heights 23,000.00	
	Cash 373.00	
	Accrued interest on bonds 482.36	
	St. Louis Heights, 2/15/30	
	to 7/16/30	273,855.36
Dec 26 1930	Bonds 107,000.00	
	Cash 67,036.12	
(a)	Interest on above \$67,036.12 cash item from July 31 to Dec 31 1930 at 2% monthly	670.36
(b)	Accrued interest on bonds 607.50	
	St. Louis Hts	
	1/2 mo \$141.67	
	Ark Power & Light	
	2 mo 91.66	
	Alabama Power	
	4 mo 166.67	
	Texas Power & Lt	
	3 mo 125.00	
	Emporium Capwell	
	Corpn 2 mos 82.50	
	\$607.50	175,313.98

Payable

in 1931 (c) Proportion of E J Lord's

1930 estimated federal
income tax assumed
and payable by E J
Lord Ltd in 1931

26,904.66

Total proceeds, per
Assessor

\$476,074.00

LESS Cost

60,000.00

Balance subject to
tax, per assessor

\$416,074.00

Adjustments

The following items should be
deducted:

(a) Interest on \$67,036.12 670.36

This interest was not part
of the redemption transac-
tion and was therefore in-
cluded on taxpayer's orig-
inal return as part of item
#3—\$9969.99

(b) Accrued interest on bonds 607.50

This interest was not part
of the redemption transac-
tion and was therefore in-
cluded on taxpayer's orig-
inal return as part of item
#3—\$9969.99

[Seal]

[2]

(c) Reduction in amount of Federal 6,576.16

Income Tax liability assumed

by E J Lord Ltd

Federal tax as originally
computed \$26,904.66

Federal tax as
amended 20,328.50

\$ 6,576.16

Legal expenses paid by E J Lord	1,650.00	
not included in assessor's computation	<u>\$ 9,504.02</u>	<u>\$ 9,504.02</u>

NET AMOUNT ACTUALLY RECEIVED BY

E. J. Lord for redemption of 600 shares of
E J Lord Ltd stock over and above the cost
of said stock

Note: The taxpayer contends that this amount represents a distribution of earnings which have already been subjected to the Territorial income tax in the hands of the corporation and that such distribution is therefore specifically exempted from tax in the hands of the taxpayer, under the Territorial Income Tax Law.

[Seal]

[3]

INCOME TAX APPEAL.

[Endorsed]: Received June 30/31, Territorial Board of Equalization.

To—Harold C. Hill, Esq.,

Assessor of Taxes,

First Division, Territory of Hawaii.

APPEAL FROM ASSESSMENT.

You are hereby notified that the undersigned, having made a return showing the gross income received from all sources during the year immediately preceding the first day of January, 1931, the amount

of deductions therefrom and the amount of taxable income for such period; and having received notice that an assessment has been made in which the amount of taxable income has been raised above the amount in said return, as follows:—

	Returned	Assessed
Gross Amount of Income.....	\$527,598.20	\$421,329.64
Deductions	534,543.78	21,705.24
Amount of Taxable Income	None	398,224.40
Tax as graduated.....		18,686.22
Totals.....		\$ 18,686.22

And deeming himself aggrieved by the changes made in the amount of taxable income whereby the amount of taxes payable by the undersigned is increased from nothing, the amount payable according to such return, to \$18,686.22, hereby appeals from such assessment to the Territorial Board of Equalization, Territory of Hawaii, basing such appeal upon the following grounds:

1.

That the assessor of the First Taxation Division failed to give the tax payer notice of his raise in the amount of taxable income above the amount stated in the return of the tax payer within the time required by law to wit, R. L. H. 1925 Sections 1348 and 1396, said assessor having failed to give the tax payer notice of such raise prior to April 25, 1931.

2.

That the tax assessor erred in computing the gross income [4] of the tax payer for the year ending December 31, 1930.

3.

That the said tax assessor erred in computing the net income of the tax payer for the year ending December 31, 1930.

4.

That the said assessor erred in computing the amount of taxable income of the tax payer for the year ending December 31, 1930.

5.

That the said assessor erred in including in the income of the tax payer and refusing to allow as a deduction the amount received by the tax payer from E. J. Lord, Ltd., an Hawaiian corporation, the sum of \$406,569.98 as dividends upon the stock of such corporation upon the net profits of which said corporation a tax of 2% had been assessed, as required by R. L. H. 1925, Chapter 103.

Dated at Honolulu, T. H. June 18, 1931.

(Sgd.) E. C. PETERS

Attorney for tax payer—E. J. Lord. [5]

Before the Territorial Board of Equalization, Territory of Hawaii, Honolulu, Hawaii.

In the matter of the Income Tax Appeal of

EDMUND J. LORD

For the year ending December 31, 1930,
First Taxation Division.

DECISION.

The Taxpayer, Edmund J. Lord, filed with the Tax Assessor, First Division, his individual income tax return for the twelve months preceding January 1, 1931, in which he claimed a deficit of \$6,945.58 and an exemption of \$1,400.00, a total deficit and exemption of \$8,345.58.

The Tax Assessor disallowed a deduction claimed by the Taxpayer amounting to \$406,569.98 and found the Taxpayer's net taxable income to be \$398,224.40 on which he imposed an income tax amounting to \$18,686.22, whereupon the Taxpayer appealed to this Board.

Prior to 1930 the Taxpayer owned 600 of the 1000 shares of stock of E. J. Lord, Ltd., and during the year 1930 delivered his stock to that Company. Before this Board the Taxpayer contended that the difference between the total amount he received from E. J. Lord, Ltd., for his 600 shares of stock and the amount of his original investment of \$60,000.00 for this stock, was a dividend, a distribution to him of 60% of the accumulated earnings or surplus of the Company; that since the net earnings

of the Company had been each year properly shown on the Company's Territorial Income Tax Return and income taxes had been levied thereon by the Tax Assessor and paid by the Company, these earnings should not again be subjected to income tax when distributed to stockholders; that, in effect, this transaction with the Company was [7] a sale and a delivery by him to the Company of his 600 shares of stock for \$60,000.00 and a dividend paid to him by the Company.

The Tax Assessor's contention was that no dividend was declared or paid in 1930 other than a dividend of \$25,000.00 regularly entered in the Company's books of record,—in which, it developed, the Taxpayer did not participate since he had delivered his stock to the company prior to the date of the declaration of this dividend of \$25,000.00,—and that the transaction was purely a sale of the Taxpayer's 6000 shares of stock to E. J. Lord, Ltd., at a price for the whole 600 shares, and that the difference between what the Taxpayer paid for the 600 shares and what he received from the Company for the transaction, upon the relinquishment of these shares by him to the Company, was taxable income upon which the Tax Assessor had properly levied an income tax.

This Board is of the opinion that the records of the Company show conclusively that the Company intended the transaction to be wholly a sale, as for example;—

(1) In the minutes of a special meeting of the Board of Directors of E. J. Lord, Ltd., held on

December 7, 1929, (Taxpayer's Exhibit 30a) the manner of the proposed purchase by the Company of the Taxpayer's 600 shares of stock is recorded with a specific provision that the Company should pay the Taxpayer 40% of the amount to which Mr. E. J. Lord may become liable for Federal and Territorial Income taxes upon income accrued and to accrue to him resulting from the sale of said 600 shares";

(2) In an agreement entered into between the Taxpayer and E. J. Lord, Ltd., on December 13, 1929, (Taxpayer's Exhibit 9) the manner of payment by the Company for the sale to it of the Taxpayer's 600 shares of stock in the Company is set forth in detail and one of the provisions of the agreement is that 40% of the amount of Federal and Territorial Income Tax upon income accruing and to accrue to the Taxpayer by reason of the "consummation [8] of the sale of said 600 shares "shall be paid by the Company to the Taxpayer "forthwith upon assessment";

(3) In the minutes of a meeting of the Board of Directors of E. E. Black, Ltd.,—successor to E. J. Lord, Ltd.,—held on December 20, 1930, (Taxpayer's Exhibit 38c) reference is again made to the agreement of the Company to pay 40% of the said taxes;

(4) In Taxpayer's Federal Income Tax return for the calendar year 1930, (Tax Assessor's Exhibit A) in Schedule D thereof, the disposition of the said 600 shares of stock is listed as a sale of capital

assets to E. J. Lord, Ltd., and a tax of 12½% was imposed on the gain;

(5) In the Annual Corporation Exhibit of E. E. Black, Ltd., for the year ending December 31, 1930, (Taxpayer's Exhibit 6f) "Treasury stock" is listed among the assets. There is no such item listed among the assets in the comparative list of assets for 1929 of the same Corporation Exhibit. No other stock than Taxpayer's 600 shares was purchased by the Company in 1930.

In a hearing before this Board on Monday, December 7, 1931, (page 117 of the transcript) E. E. Black testified that it was the intention of E. J. Lord, Ltd., to redeem the capital stock held by the Taxpayer "because it was representing my ambition of a life-time to own my own company".

In arguing the case before this Board, counsel for E. E. Black (pages 202-203 of the transcript) contended that there was a distribution to E. J. Lord of 60%, his interest in the profits of the corporation and his original contribution of capital; that, inasmuch as E. E. Black was left in the corporation and owning every share of the corporation, this was a distribution, that the transaction "was a distribution between Johnny Black on the one hand and Mr. Lord on the other". [9]

This Board disagrees with the above contention. The Board holds that on December 31, 1930, E. E. Black, Ltd., and not E. E. Black was the owner of the 600 shares purchased from the Taxpayer; that E. E. Black's ownership of stock was limited

to 40%—less the two or three shares nominally held by the other directors—and that there had been no distribution to E. E. Black.

The Taxpayer cannot be permitted to come in now and maintain the claim that the transaction was a dividend, a distribution of surplus upon which no further Territorial Income Tax should be paid, while the records of the Company fail to show that E. E. Black the 40% stockholder, received as an individual any portion of the distribution. The records do show that a sale was intended and was consummated.

In cross-examination before this Board of H. Glass, head of the Territorial Income Tax Bureau, counsel for E. E. Black (page 166 of the transcript) contended that no Territorial Income tax would have accrued had the Company taken what he called “the long way round, the red-tape proposition” of declaring and paying a dividend to both the Taxpayer and E. E. Black, but he failed to state the very obvious fact that had the Company so acted, both the Taxpayer and E. E. Black would have received dividends of such large amounts that the sum of their Federal surtaxes accruing on the same would have greatly exceeded the amount of the Federal Tax actually paid by the Taxpayer on his gain on the sale of capital assets, plus the amount of the Territorial Income tax levied in 1931 against the Taxpayer.

This Board finds for the Tax Assessor and hereby decides that the Taxpayer had for the twelve months

preceding January 1, 1931 a taxable income of \$398,224.40, on which a territorial income tax amounting to \$18,686.22 shall be paid. [10]

TERRITORIAL BOARD OF EQUALIZATION

(Sgd.) CHAS. T. WILDER

Chairman,

(Sgd.) JOHN J. WALSH

Member,

(Sgd.) ANDREW ADAMS

Member.

Honolulu, Hawaii.

January 20, 1932. [11]

[Title of Court and Cause.]

APPEAL AND NOTICE OF APPEAL.

Comes now, Edmund J. Lord, the taxpayer in the above entitled matter, and hereby gives notice of appeal and does hereby appeal to the Supreme Court of the Territory of Hawaii from the decision of the Territorial Board of Equalization, Territory of Hawaii, made and entered in the above entitled matter on the 20th day of January, 1932, finding for the Tax Assessor, First Division, Territory of Hawaii, and against the Taxpayer and deciding that said taxpayer had for the twelve months preceding January 1, 1931 a taxable income of \$398,224.40 on which the Territorial income tax amounted to \$18,286.22 shall be paid; and said taxpayer prays that all of the records in said matter, together with

the reporter's transcript of evidence, all exhibits and all other evidence, and this Notice of Appeal and Appeal, be forwarded to the Clerk of the Supreme Court of the Territory of Hawaii.

Dated: Honolulu, Territory of Hawaii, this 29th day of January, 1932.

EDMUND J. LORD

By PROSSER, ANDERSON,
MARX & WRENN

His Attorneys.

By (Sgd.) HEATON L. WRENN

The service of a copy of the
within

Appeal & Notice of Appeal
this day admitted

Dated Jan. 30

(Sgd.) H. T. KAY

Attorney for Assessor [13]

[Endorsed]: Filed February 1, 1932, at 11:40
o'clock a. m. (Sgd.) Robert Parker, Jr., Clerk
Supreme Court. [12]

[Title of Court and Cause.]

CERTIFICATE.

I hereby certify that the above entitled matter was heard before this Board on the Taxpayer's appeal from the assessment of the Tax Assessor, First Division, and that the Taxpayer now appeals to the Supreme Court of the Territory of Hawaii

from the decision of this Board finding for the Tax Assessor; that

- (1) Net taxable income found by the Assessor, \$398,224.40 and tax thereon \$18,686.22;
- (2) Net taxable income returned by Taxpayer, none and tax thereon none;
- (3) Net taxable income fixed by this Board, \$398,224.40 and tax thereon \$18,686.22;
- (5) Points of law, none.

I further certify that the following constitute all of the records before this Board in the above case and submit same herewith:—Taxpayer's return, Notice of Assessment by Assessor, Decision of this Board, 238 pages of the transcript of evidence, Exhibits "A to E-3" inclusive of the Assessor, Exhibits "1 to 38-c" of the Taxpayer, Appeal and Notice of Appeal together with Statutory costs in the amount of \$1,106.56 and letter from Messrs. Prosser, Anderson, Marx and Wrenn, Attorneys for Taxpayer protesting the payment to this Board of the Statutory costs.

Witness my hand this first day of February 1932.

(Signed) CHAS. T. WILDER

Chairman,
Territorial Board of Equalization,
Territory of Hawaii. [14]

No. 2052.

In the Supreme Court of the Territory of Hawaii.

October Term, 1933.

Appeal from Territorial Board of Equalization.

In the Matter of the Income Tax Appeal
of

EDMUND J. LORD,

For the year ending December 31, 1930,
First Taxation Division.

OPINION OF THE COURT.

[Endorsed]: Filed Dec. 2, 1933 at 9:40 o'clock
a. m. (Sgd.) Robert Parker, Jr., Clerk Supreme
Court. [15]

Argued October 26, 1933.

Decided December 2, 1933.

PERRY, C. J., BANKS AND PARSONS, JJ.

Taxation—income tax—profits from sale of movable property.

When all of the stock of a corporation is held by two persons and one of the stockholders sells to the corporation and the corporation repurchases from him all of his stock for an agreed consideration larger than the amount originally contributed by the seller for the stock, the resulting gain to the stockholder is taxable as income, even though a part of the consideration paid by the corporation was derived from undistributed profits upon which it had already paid an income tax of two per cent.

Upon the facts and evidence recited in the opinion, *held*, that the transaction between one of two sole stockholders and the corporation was a sale by him and a repurchase by it and was not and did not include a payment in the nature of a dividend by the corporation to the stockholder. [16]

Same—same—taxation period—time of accrual of profits.

Under sections 1388 and 1391, R. L. 1925, the profits resulting to a stockholder from the sale of his stock are taxable as income of the year during which the sale was made irrespective of whether or to what extent the increase in value in reality accrued during preceding years.

Same—profits from sale—dividends—intention of parties.

In determining whether a transaction relating to the transfer of all of his stock by the holder thereof to the corporation and the acquisition of the same by the corporation was a sale by the stockholder and a repurchase by the corporation or was, in part at least, the payment of a dividend out of undistributed profits which had already borne an income tax of two per cent, the question is one largely of the intention of the parties who took part in the transaction. [17]

OPINION OF THE COURT BY PERRY, C. J.

This is an appeal from the decision of the board of equalization sustaining an assessment against E. J. Lord, the appellant, of an income tax upon certain moneys received by him during the year preceding January 1, 1931.

E. J. Lord and E. E. Black, having been prior thereto associated in the contracting and building business, in September, 1926, formed a corporation under the name of E. J. Lord, Limited. The corporation had a capital stock of \$100,000 in one thousand shares, six hundred shares of which were issued to E. J. Lord and four hundred shares to E. E. Black, Lord contributing in payment of the stock money or other capital of the value of \$60,000 and Black contributing money or other capital of the value of \$40,000. Apparently to comply with the requirements of the law relating to the formation of corporations, three other stockholders were named, each as the holder of one share, but, as testified to by Black at the trial before the board, these three held the shares only "nominally" and were in reality "dummies." In each of the annual reports subsequently filed with the treasurer of the Territory only two persons were named as holders of the capital stock and these were E. J. Lord as holding six hundred shares and E. E. Black as holding four hundred shares.

The corporation met with a large measure of success and received substantial profits from its operations.

Late in 1929 E. E. Black, whose ambition had long been to form and control a corporation of his own, and E. J. Lord, who, because of ill health and perhaps for other reasons, desired to retire from the active pursuit of that business, after various discussions came to the understanding that Lord would retire and [18] that Black would continue the business. On December 13 of that year they signed a written document which had been prepared by learned counsel, a former chief justice of this court, stating the terms of the understanding which the two had so reached. There was included in the agreement the grant to E. J. Lord Company, Limited, of an option to acquire the six hundred shares owned by E. J. Lord, for a consideration therein stated. Shortly thereafter the option was accepted by the corporation and in due course, in part early in 1930 and in part in December of 1930, the sum of \$468,219.98 was paid to Lord in accordance with the terms of the contract.

Subsequent to the acceptance of the option the name of the corporation was changed to E. E. Black, Limited, and its capital stock was reduced to \$40,000 divided into four hundred shares, all of which was held by E. E. Black. Section 1391, R. L. 1925, which is part of chapter 103, relating to income taxes, provides that "in assessing the income of any person or corporation there shall not be included the amount received from any corporation as dividends upon the stock of such corpora-

tion if the tax of two per centum has been assessed upon the net profits of such corporation as required by this chapter." It is undisputed that the money paid to E. J. Lord under the contract referred to, other than the sum of \$60,000 which came from capital, was actually paid by the corporation out of undivided profits, partly earned prior to the date of the contract and partly earned after the date of the contract and that upon all of these undivided profits the corporation had paid the tax of two per cent required by law. The contention of the taxpayer-appellant is that the moneys received by him in 1930 (other than \$60,000 thereof) were received by him "as a dividend" out of profits which had already borne the statutory tax of two [19] per cent and are, therefore, exempt from taxes as income of E. J. Lord. The contention of the Territory, on the other hand, is that in the transaction between Lord and Black there was not any payment of a dividend and that there was simply a sale by Lord and a purchase by the corporation of the six hundred shares of the capital stock owned by Lord and a payment therefor of the purchase price in which was not involved or included any idea of a dividend. A second claim by the appellant is that even if the moneys in question were not received by Lord "as a dividend" but are to be deemed gains or profits derived from the sale of personal property, still no tax is assessable thereon because the increase in value of the six hundred shares over and above \$60,000 accrued during the years 1926,

1927, 1928 and 1929 and did not accrue wholly during the taxation year of 1929.

The main question is, what was the nature of the transaction between the corporation and Lord? As to the \$60,000 there is no dispute. It was a restoration to Lord of the capital which he had contributed. As to the remainder, was it received by Lord as a dividend? The board of directors of E. J. Lord, Limited, held a meeting on December 7, 1929, to consider the proposal then pending. Under the title of "Purchase of Stock" the minutes of that meeting say: "Mr. E. E. Black moved that as Mr. E. J. Lord was willing to sell all his stock of E. J. Lord, Ltd., the company was to redeem the 600 shares for which the company was to pay for the said shares in the following manner: (1) The sum of money equal to 60% of the net worth of the company as of December 31st, 1929; (2) the sum of money equal to 60% of the net profits of all contracts awarded and not completed on December 31, 1929; (3) the sum of money equal to 40% of the amount to which Mr. E. J. Lord may become liable for federal and territorial income taxes upon [20] income accrued and to accrue to him resulting from the sale of said 600 shares. Mr. Lord agreed to give the company an option to purchase the above mentioned stock to February 28th, 1930, and to have an agreement drawn signed by both parties covering the above option, price and payments to be made, a copy of such agreement to be entered into the minute book." This motion

carried unanimously. Another motion adopted at the same meeting was: "That the company upon the exercise of the option cause its articles of association to be amended" so as to effectuate a change of name.

Then followed the carefully drawn agreement of December 13, 1929, which was intended as appears from the evidence, to be a written record of what the agreements were. Omitting irrelevant portions, that instrument recited and declared, referring to E. J. Lord's six hundred shares of capital stock, that the corporation "desires to redeem said shares of stock;" that Lord "is willing to accept as consideration for the sale of said stock" to the corporation and the corporation "is willing to pay" to Lord "for the redemption of said stock, a sum of money equal to sixty per cent (60%) of the net worth" of the corporation "as of December 31, 1929, and a sum of money equal to sixty per cent (60%) of the net profits yet to accrue" to the corporation "by its completion of the respective works contemplated by certain executory contracts to which" the corporation "is a party, remaining uncompleted, and the further sum of money equal to forty per cent (40%) of the amount to which" Lord "may become liable to the United States of America and/or the Territory of Hawaii for income taxes upon income accrued and/or to accrue to him by reason of and resulting from the exercise" by the corporation "of the option hereby granted and the consummation of the sale of said six hundred (600) shares of the capital stock" of the corpora-

tion; that "the net worth of the" corporation "cannot be [21] determined until the books" of the corporation "have been closed for the year 1929 and an audit made thereof;" that certain enumerated contracts were uncompleted; that therefore Lord "does hereby * * * " (a) "give and grant" to the corporation "an option, irrevocable within the time for acceptance herein limited, to purchase free from encumbrances the said six hundred (600) shares of the capital stock" of the corporation "so owned by him * * * for the consideration hereinafter set forth," (b) "assign and deliver" to the corporation the same six hundred shares, duly endorsed, "by way of pledge to secure the performance" of Lord's covenants and (c) appoint the corporation his attorney "upon the exercise of the option hereby granted" to cause the said six hundred shares "of the capital stock * * * to be redeemed" by the corporation and "to be recorded on the proper books" of the corporation. The corporation, on the other hand, agreed (1) to close its books as of December 31, 1929, and to have them audited, (2) to faithfully complete the uncompleted contracts in as economical manner as possible, (3) to have its books open to the inspection of Lord at all times and (4) that "upon the exercise of the option by it to it hereby granted," it will, "as soon as may be, cause its articles of association to be amended" so as to effectuate the desired change of name. Both parties mutually covenanted and agreed therein (1) that "the option

hereby given shall be open for acceptance up to, but not after the 28th day of February, 1930," (2) that "the purchase price of the said stock" should be, reciting the precise language earlier in the document used, "a sum of money equal to sixty per cent (60%) of the net worth" of the corporation as of December 31, 1929, "a sum of money equal to sixty per cent (60%) of the net profits yet to accrue" to the corporation "by its completion" of the uncompleted contracts and "the further sum of money equal to forty per cent [22] (40%) of the amount" which Lord "may become liable" to pay "for income taxes upon income accrued and to accrue to him by reason of and resulting from the exercise" by the corporation "of the option hereby granted and the consummation of the sale" of the six hundred shares. The document further recites "that such purchase price shall be paid" to Lord as follows: "The sum of money equal to sixty per cent (60%) of the net worth" of the corporation "as of December 31, 1929, forthwith upon the exercise" by the corporation "of the option hereby granted to it. In the event that the amount so payable exceeds the sum of two hundred fifty thousand dollars (\$250,000.00), the amount of the excess over that sum may be retained" by the corporation "until and paid by it to" Lord "upon the completion of the St. Louis Heights contract and the receipt by it of the full consideration for the performance thereof, the sum of money equal to sixty per cent (60%) of the net profits yet to accrue from each of the foregoing enumerated uncompleted contracts

when completed and the moneys, bonds or other consideration accrued and payable or deliverable" to the corporation "thereunder, reduced to possession, and the sum of money equal to forty per cent (40%) of the income tax" which Lord might become liable to pay "for income taxes upon income accrued or to accrue to him by reason of and resulting from the exercise by" the corporation "of the option hereby granted and the consummation of the sale" of the six hundred shares "forthwith upon assessment."

Under date of February 15, 1930, Lord signed a paper whereby he acknowledged receipt of the sum of \$250,000 in money or its equivalent, from the corporation, which paper read as follows: "E. J. Lord, Limited having duly accepted the option granted by me to it by the indenture of agreement between us dated December 13, 1929, and the sum of two hundred seventy-three thousand eight [23] hundred fifty-five dollars and thirty-six cents (\$273,855.36) having been found to be sixty (60%) of the net worth of E. J. Lord, Limited, as of December 31, 1929; I hereby accept in lieu of cash and acknowledge receipt from E. J. Lord, Limited, in payment of the sum of two hundred fifty thousand dollars (\$250,000.00) on account of the purchase price of the six hundred (600) shares of the capital stock of E. J. Lord, Limited, the subject of said indenture, the following enumerated notes, bonds and cash,"—followed by an enumeration of the property transferred and received.

These are the formal documents which the parties executed as setting forth the terms of the transaction. Nowhere is there the slightest reference to a dividend declared, paid or received. Nowhere in the books of the corporation, as exhibited in evidence, is there any treatment of these payments to Lord or of any part thereof as a dividend or dividends. (The books do contain entries showing the payment of dividends during the four-year period.) The essence of the transaction, as disclosed by the minutes of the corporation, by the formal memorandum of contract, by the formal receipt and by the testimony, is that Lord sold to the corporation and that the corporation bought back (that is what the word "redeem" means) from him the six hundred shares of stock. There is nothing in the use of the word "redeem" or of the word "redemption" that indicates the making or the receiving of a dividend. It simply imports, as used in connection with these shares of capital stock, that the corporation which once issued or gave out the stock repurchased it or bought it back. Its use is entirely consistent with the statement in the same contract that Lord was *selling* the stock and does not in any wise qualify the use of the word "sale".

Counsel for the appellant urges that the ultimate result [24] to the parties would have been the same if the corporation had on one day declared and paid a dividend of sixty per cent of its undistributed profits and then on the next week or the next day bought Lord's six hundred shares for the sum of

\$60,000. That may be assumed to be a correct statement; but it does not affect the conclusion which ought to be reached in this case. It is not for us to consider now what the parties might have done. What is before us for consideration is, what did they actually do? This is necessarily, in large measure, a question of the intention of the parties. The instruments and records above recited are susceptible of only one interpretation in that respect and that is that the parties understood and intended that Lord was selling and that the corporation was buying the six hundred shares. Not only was there no reference to a dividend in the records evidencing the transaction but the statements made tend to exclude and to render impossible the thought of a dividend. The parties declared that it was a sale and a purchase; they declared that a part of the consideration should be a sum of money equal to sixty per cent of "the net worth of the corporation," which net worth must have necessarily included capital as well as the undistributed profits, and they did not, in that connection, distinguish between the two; that another part of the consideration was to be a sum of money equal to sixty per cent of the net profits to accrue in the future from contracts then uncompleted. They did not say that it should be sixty per cent of the net profits but did say that it should be a sum of money equal to sixty per cent of the net profits. Was the corporation on December 13, 1929, declaring a dividend out of profits not yet earned and which might not be earned for a

year longer? Moreover, in the transaction the corporation did not pay any money or deliver [25] any equivalent property to Black. He certainly did not receive any dividend. While it may be legally possible for one only of two shareholders to receive a dividend the other consenting to defer his dividend to a later time, that arrangement, when claimed to exist, should at least be shown by clear and convincing evidence; and in the case at bar there is no evidence whatever of any such arrangement. A dividend could as well have been paid to Black and the money by him later reinvested in his corporation but that is not the course that was followed.

Another consideration, not controlling and yet relevant, is that the exemption provided for in the provisions of section 1391, above quoted, is that in favor of amounts received from a corporation "as dividends *upon the stock*"* of that corporation. This would seem to presuppose the payment of a dividend to one who holds stock rather than to one who by the very transaction is relinquishing the stock to the corporation. If the legal possibility of one who is relinquishing stock in the same transaction receiving a dividend upon that stock is not excluded, at least it would require some evidence on the part of the parties to the transaction to indicate that some or all of the moneys paid to the out going stockholder were being paid as a dividend. There are no such indications in the case at bar.

*Italics by the Court.

The conclusion is irresistible that irrespective of what the parties might have accomplished if they had pursued a different course, the transaction as it actually occurred was a sale and purchase and resulted in a profit to Lord in the sale of his stock.

The other contention of appellant likewise cannot be sustained. Section 1388, R. L. 1925, provides that "there shall be levied, assessed, collected and paid annually upon the gains, profits and income received by every individual residing in the Territory, from all property owned, * * * a tax in accordance with the follow- [26] ing schedule on the amount so received during the taxation period." The schedule of rates of taxation follows. Section 1390 provides that "in estimating the gains, profits and income of any person or corporation, there shall be included * * * the amount of sales of all movable property, less the amount expended in the purchase or production of the same * * * and all other gains, profits and income derived from any source whatsoever during said taxation period." In the face of this language of the statute, the contention that the profits resulting from the sale of stock were not taxable in January, 1931, because they did not wholly accrue during the year 1930, is untenable. The requirement of the statute was that in January, 1931, liability would accrue for taxes on income which was "received" or "derived" during the taxation period, which was the year 1930; and this is made even more clear with reference to the sales of movable property when the statute de-

clares that in estimating the profits “there shall be included * * * the amount of * * * less the amount expended in the purchase.” The legislature did not, in this connection, make any exception of those parts of the gain in value which did not accrue during the taxation year and the court cannot now make the exception.

Reliance is had by the appellant upon the case of *Gray v. Darlington*, 15 Wall. 63, 65. That case was decided upon the federal statute of 1867, which taxed certain classes of income “*for** the year” preceding the taxation date. Income or gains or profits “for” a stated year can well be held to exclude gains or profits accruing during other years. This distinction was pointed out by the same court in *Hays v. Gauley Mt. Coal Co.*, 247 U. S. 189, 191, 192. The latter case was decided under the Act of 1909, which taxed “the entire net income * * * received by it” (the taxpayer) “*during** [27] such year,” which is the equivalent of the expression used in our statute for the admeasurement of taxable income. It was held in the *Hays* case that the Act of 1909 “measured the tax by the income received within the year for which the assessment was levied, whether it accrued within that year or in some preceding year while the Act was in effect,”—with an exception not material to the case at bar. And see *Ewa Plantation v. Wilder*, 26 Haw. 299, in which it was held that a sum received by the

*Italics by the Court.

taxpayer in liquidation of losses or damage sustained in consequence of a laborers' strike is to be regarded as income of the year in which it is received and may not be attributed to the years in which the damaged crops of cane were sold.

The decision of the board of equalization is affirmed.

(Sgd.) ANTONIO PERRY.

(Sgd.) JAS. J. BANKS.

(Sgd.) CHARLES F. PARSONS.

H. L. Wrenn (Prosser, Anderson,
Marx & Wrenn on the briefs) for
taxpayer.

E. C. Peters for E. E. Black, Ltd.

H. T. Kay, First Deputy Attorney General,
for the assessor. [28]

[Title of Court and Cause.]

JUDGMENT.

[Endorsed]: Filed Jan 25, 1934 at 2:45 o'clock
p. m. (Sgd.) Robert Parker, Jr., Clerk Supreme
Court. [29]

The above entitled cause having been argued on
the 26th day of October, 1933, by H. L. Wrenn,
Esq., Attorney for the taxpayer, and having hereto-
fore been submitted on briefs by E. C. Peters,
Esq., attorney for E. E. Black, Limited, and H. T.
Kay, Esq., First Deputy Attorney General, attorney
for the tax assessor, and the court having hereto-

fore on, to-wit, the 2nd day of December 1933, rendered its decision herein in favor of the tax assessor and against the taxpayer, now, therefore, pursuant to and in conformity with said decision,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED that the decision of the board of equalization is affirmed.

Dated at Honolulu, T. H., this 25th day of January 1934.

BY THE COURT:

(Sgd.) ROBERT PARKER, JR.,
Clerk.

[Seal]

Approved:

(Sgd.) ANTONIO PERRY,
Chief Justice.

O. K. as to form

Prosser, Anderson, Marx & Wrenn
E. C. Peters. [30]

[Endorsed] Filed February 1, 1932 at 11:40 o'clock a. m. Robert Parker, Jr., Clerk, Supreme Court.

Before the Territorial Board of Equalization
Territory of Hawaii.

[Title of Cause.]

TRANSCRIPT OF EVIDENCE.

The above entitled matter came duly on for hearing before the aforesaid Board on Friday, December 4, 1931, at 9:15 o'clock a. m., the Chairman,

the Honorable Charles T. Wilder, and the Honorable John J. Walsh, being present,

Harold T. Kay, Esq., Deputy Attorney General, appearing for the Tax Assessor, and

Heaton L. Wrenn, Esq., of the firm of Messrs. Prosser, Anderson, Marx and Wrenn, appearing for the Taxpayer, E. J. Lord, and

E. C. Peters, Esq., appearing for E. E. Black, Limited.

WHEREUPON the following proceedings were had and testimony taken:

Mr. KAY: Is the Board ready to go ahead?

M. WALSH: We are ready. We have a reporter to make a transcript.

Mr. WRENN: We have some preliminary matters. I see no reason we cannot go ahead.

Mr. KAY: Well, if the Board cares to go ahead at this time, I have no objection.

The CHAIRMAN: Mr. Adams can read the transcript afterwards. [31]

Mr. KAY: I have asked Mr. Nye to bring certain papers in regard to E. J. Lord, Limited, and E. E. Black, Limited. Have you the original articles of incorporation of E. J. Lord, Limited?

Mr. NYE: Yes.

Mr. WRENN: I offer in evidence at this time, on behalf of the taxpayer, the original articles of association of E. J. Lord, Limited, filed in the office of the Treasurer of the Territory of Hawaii on September 7, 1926.

Mr. KAY: May I see what you have?

Mr. WRENN: May the original articles of association and affidavit of incorporation attached thereto, and Exhibit "A," be admitted as one exhibit.

(Documents offered in evidence received and marked: "Taxpayer's Exhibit 1.")*

Mr. WRENN: May the petition for the amendment of the articles of association, changing the name from E. J. Lord, Limited, to E. E. Black, Limited, dated February 15, 1930, together with the certificate of the presiding officer attached thereto, the allowance of amendment, which is likewise attached thereto in this file, and the certificate for filing with the Registrar of Public Conveyances with the Treasurer be admitted as Exhibit 2 for Taxpayer?

(Documents offered in evidence received and marked: "Taxpayer's Exhibit 2.")*

Mr. WRENN: And may the application for reduction of [32] capital stock of E. E. Black, Limited, filed in the Treasurer's office March 12, 1931, the application being dated March 7, 1931, together with the certificate of the officers of E. E. Black, Limited, on the reduction of capital stock attached thereto, and Exhibit "A" attached to the application showing the resolution of the shareholders, which is likewise attached thereto,—

Mr. KAY: Is there a reduction of stock made in 1931?

*Omitted from printed record on stipulation by counsel.

Mr. WRENN: Yes.

Mr. KAY: We will have to object.

Mr. WALSH: What does the reduction in capital in 1931 have to do with that?

Mr. WRENN: It has a great deal to do. We will show that at the time the original transaction was entered into between Taxpayer and E. J. Lord, Limited, it was the intention of E. J. Lord, Limited, to redeem this stock, and when it was redeemed from Mr. Lord to apply for the reduction of the stock of the company and cancellation of the stock, and that was duly carried out. We will show that the final payment on the amount which was to be made to Mr. Lord was not made until December 31, 1930. Subsequently in 1931 there was an adjustment to E. E. Black, Limited, on account of Federal income taxes, and immediately thereafter E. E. Black, Limited, applied for a reduction of the capital stock, which [33] application was granted, so it is very important.

Mr. KAY: If that bears on the 1930 income, we will withdraw our objection. We have no intention to object to anything relating to the 1930 income.

Mr. WRENN: Together with the affidavit of the notice to the Treasurer and approval of the reduction of the stock by the Treasurer on March 31, 1931.

(Documents offered in evidence received and marked: "Taxpayer's Exhibit 3.")

TAXPAYER'S EXHIBIT 3

APPLICATION FOR REDUCTION OF CAPITAL STOCK OF E. E. BLACK, LIMITED.

To: The Honorable E. S. Smith, Treasurer of the Territory of Hawaii:

E. E. Black, Limited, a Hawaiian corporation, with a capital stock of \$100,000. divided into 1,000 shares of the par value of \$100. each, desires to reduce its capital stock to \$40,000. divided into 400 shares of the par value of \$100. each by retiring 600 shares of the par value of \$100. each, and herewith presents a sworn certificate as required by law signed by the presiding officer and secretary of an Annual meeting of stockholders of said corporation held on the Seventh day of March, 1931, showing what action was taken in the premises at said meeting.

The said corporation prays that you publish in a suitable newspaper in Honolulu a notice of said certificate as required by law, and after the time allowed by law has elapsed that you allow said reduction of capital of said corporation and enter the same of record, and that you do approve the retirement and cancellation of 600 shares of the par value of \$100. each with an aggregate par value of \$60,000.

Dated at Honolulu, T. H., March 7th, 1931.

E. E. BLACK, LIMITED,

By (signed) E. E. BLACK

Presiding Officer of said meeting

[Seal]

By (signed) T. IKEJIRI

Secretary of said meeting.

No. 2052. Filed February 1, 1932 at 11:40 o'clock a. m. (s) Robert Parker, Jr., Clerk Supreme Court. [264]

CERTIFICATE ON REDUCTION OF CAPITAL
STOCK OF E. E. BLACK, LIMITED.

Territory of Hawaii

City and County of Honolulu.—ss.

E. E. BLACK and T. IKEJIRI respectively duly sworn on oath, depose and say:

That the said E. E. Black was the presiding officer and said T. IKEJIRI was the Secretary of an Annual meeting of stockholders of E. E. Black, Limited, a Hawaiian corporation, duly convened in Honolulu, City and County of Honolulu, Territory of Hawaii, on the 7th day of March, 1931, for the purpose of considering a reduction of the capital stock of said corporation;

That at the time of said meeting the capital stock of said corporation consisted of 1,000 shares of the par value of \$100. each and of the aggregate par value of \$100,000.;

That at said meeting there were present or represented by proxy owners and holders of 1,000 shares, being all of the issued capital stock of said corporation, of which 600 shares were held in the treasury of said corporation, and all of the shares present or represented at said meeting voted for and in favor of a resolution to reduce the capital stock of the Company from \$100,000, to \$40,000 by retiring 600 shares of the par value of \$100. each of said corporation now held in the treasury;

That attached hereto and marked Exhibit "A" and made a part hereof is a true and correct copy of the resolution duly adopted and passed at said

meeting by a vote of all of the shares of the capital stock of said corporation;

That at the time of said meeting the assets of said corporation had a book value of \$174,958.63 and the said corporation owed, exclusive of its liability to its stockholders, the sum of \$7,149.86, and that said corporation was not then and has not since become otherwise indebted in any [265] manner over and above half the amount of \$40,000. which will be the remaining capital stock of said corporation after the proposed reduction has been effected.

(Signed) E. E. BLACK

(Signed) T. IKEJIRI

Subscribed and sworn to before me this 12th day of March, 1931.

[Seal]

(Signed) H. EDMUNDSON

Notary Public, First Judicial Circuit,
Territory of Hawaii. [266]

EXHIBIT "A"

E. E. BLACK, LIMITED

—Reduction of Capital Stock—

"WHEREAS E. E. Black, Limited, has an authorized capital stock of \$100,000. divided into 1,000 shares of the par value of \$100. each and has purchased from one of its stockholders 600 of said shares of the par value of \$100. each of the aggregate par value of \$60,000. and has paid for the same and holds the same in its treasury and desires to retire said 600 shares and to reduce its capital stock accordingly to \$40,000. divided into 400 shares of the par value of \$100. each,

“THEREFORE BE IT RESOLVED that the authorized capital stock of E. E. Black, Limited, be reduced from \$100,000. divided into 1,000 shares of the par value of \$100. each to \$40,000. divided into 400 shares of the par value of \$100. each by retiring 600 shares of the par value of \$100. each now held in the treasury;

“That a sworn certificate signed by the presiding officer and secretary of this meeting be presented to the Treasurer of the Territory of Hawaii setting forth therein the action taken and certifying that at the time the vote on this resolution was taken the corporation was not and has not since become indebted in any manner over and above half of the amount of its remaining capital stock;

“AND BE IT FURTHER RESOLVED that when the said reduction of capital stock is effected as required by law, the Treasurer of this corporation do retire and cancel the said 600 shares of the par value of \$100. each of this corporation now held in the treasury.” [267]

OFFICE OF THE TREASURER,
TERRITORY OF HAWAII.

Notice of the Reduction of the Capital Stock of
E. E. BLACK, LIMITED.

Notice is hereby given the E. E. BLACK, LIMITED, a corporation organized and existing under and by virtue of the laws of the Territory of Hawaii, has pursuant to law in such cases made and provided, duly filed in the office of the Treasurer of the Territory of Hawaii a sworn certificate, as re-

quired by law, showing the reduction of the capital stock of said corporation from a total amount of \$100,000.00, divided into 1,000 shares of the par value of \$100.00 each, to a total amount of \$40,000.00, divided into 400 shares of the par value of \$100.00 each.

Notice is further given hereby to all stockholders and creditors of said corporation, and to all persons claiming to be stockholders or creditors of said corporation, or otherwise interested therein, that all protests and objections to such reduction of capital stock must be filed in the office of the Treasurer of the Territory of Hawaii before the expiration of thirty days from the 17th day of March, 1931, (the date of the first publication of this notice) to be entitled to consideration.

Dated at Honolulu, T. H., March 16, 1931.

(Signed) E. S. SMITH

Treasurer, Territory of Hawaii.

HONOLULU STAR-BULLETIN: Publish the above notice in your issues of March 17, 24, 31, April 7, 14, 1931. Send bill to E. E. BLACK, Ltd., Pohukaina St., Honolulu, T. H. File AFFIDAVIT OF PUBLICATION in Office of Territorial Treasurer immediately after last publication. [268]

Territory of Hawaii,
Island of Oahu.—ss.

Before me, the undersigned, a Notary Public, this day personally came NELSON G. PRINGLE, who

being first duly sworn, according to law, says that he is the bookkeeper of the HONOLULU STAR-BULLETIN, a newspaper published at Honolulu, Territory of Hawaii, daily, except Sundays and that the ordered publication of

NOTICE OF REDUCTION CAPITAL

STOCK E. E. BLACK LTD.

was published in said paper on the following dates:
—MARCH 17-24-31 APRIL 7-14-, A. D. 1931.—

(Sgd.) Nelson G. Pringle

HONOLULU STAR-BULLETIN.

Subscribed and sworn to before me this 15th day of April, A. D. 1931.

[Seal]

(Sgd.) WM. J. FORBES

Notary Public, in and for the First
Judicial Circuit, Oahu, Territory
of Hawaii. [269]

OFFICE OF THE TREASURER OF THE
TERRITORY OF HAWAII.

In the Matter of the Reduction of the Capital Stock
of E. E. BLACK, LIMITED.

ORDER APPROVING REDUCTION
OF CAPITAL STOCK.

WHEREAS, at an annual meeting of the stockholders of E. E. BLACK, LIMITED, a Hawaiian corporation, duly called and held in Honolulu, City and County of Honolulu, Territory of Hawaii, on the 7th day of March, 1931, at which meeting there were present or represented by proxy owners and holders of 1,000 shares, being all of the issued cap-

ital stock of said corporation, of which 600 shares were held in the Treasury of said corporation, it was unanimously voted by said stockholders to reduce the capital stock of said corporation from a total amount of \$100,000.00 divided into 1,000 shares of the par value of \$100.00 each, to a total amount of \$40,000.00, divided into 400 shares of the par value of \$100.00 each; and

WHEREAS, a sworn certificate, as required by law, was on the 12th day of March, A. D. 1931, presented to the undersigned, setting forth therein the action taken at said meeting, and certifying that at the time said vote was taken said corporation was not and has not since become indebted in any manner over and above half of the amount of its remaining capital stock; and

WHEREAS, notice of said certificate and of such reduction of capital stock was published in a suitable newspaper, to wit: The Honolulu Star-Bulletin, in Honolulu, City and County of Honolulu, Territory of Hawaii, on to wit: the 17th, 24th and 31st days of March and the 7th and 14th days of April, 1931; and

WHEREAS, thirty days have expired since the first publication of [270] said notice and no protest or objection to such reduction of capital stock has been filed with the undersigned by any person claiming to be a stockholder or creditor of said corporation or any other person; and

WHEREAS, the undersigned is satisfied that the vote so certified was truly taken, and that said

corporation was not at the time of filing said certificate indebted beyond the limit aforesaid, and that there is no objection to such reduction of capital stock; and

WHEREAS, the fee required by law in such cases has been paid by said corporation;

NOW, THEREFORE, IT IS HEREBY ORDERED that such reduction and decrease of capital stock be and the same is hereby approved and allowed and entered of record in this office and that such reduction and decrease shall stand effected as of the date of the original filing of said certificate, to wit: the 12th day of March, A. D. 1931.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of the Treasurer's Office, Territory of Hawaii, at Honolulu, T. H., this 29th day of May, A. D. 1931.

[Seal]

(Signed) E. S. SMITH

Treasurer, Territory of Hawaii.

Decrease of Capital \$25.

Recording 1,500 wds 7.50

\$32.50

(Signed) HENRY A. NYE

Registrar of Public Accounts. [271]

Territory of Hawaii

Honolulu, Oahu.

OFFICE OF THE TREASURER.

I, E. S. SMITH, Treasurer of the Territory of Hawaii, do hereby certify that the foregoing is a true and correct copy of the Reduction of Capital

Stock of E. E. BLACK, LIMITED, reducing its capital from \$100,000.00 to \$40,000., by dividing into 400 shares of the par value of \$100. each, as on record in this office.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of the Treasurer's Office, Territory of Hawaii, at Honolulu, T. H., this 30th day of January, A. D. 1932.

[Seal]

(Signed) E. S. SMITH

Treasurer, Territory of Hawaii. [272]

Mr. WRENN: We offer in evidence as Exhibit 4 a record of the Treasurer's office showing the date of articles of incorporation September 3, 1926, (Sept. 7),

date of incorporation October 27, 1926, of E. J. Lord, Limited, and showing a capital stock of one hundred thousand dollars, filing number 1831.

(Document offered in evidence received and marked: "Taxpayer's Exhibit 4.")*

Mr. WRENN: We would like to substitute this later on with copies,—and further record of E. E.

(12)

Black, Limited, showing that on March 1, 1931, its capital was forty thousand dollars.

(Document offered in evidence received and marked: "Taxpayer's Exhibit 5.")

*Omitted from printed record on stipulation by counsel.

TAXPAYER'S EXHIBIT 5

Advertiser 166848 Recorded		Date of Charter Or Articles	Date of Incorporation	Date of Dissolution	Existence Years	Limit of Capital		Present Capital											
Book No.	Folio					Date	Amount	Date	No. Shares	Par Value	Amount								
37	78																		
43	189	Sept. 3, 1926	Sept. 7, 1926		50	Sept. 3 1926	1,000.00	Sept. 3, 1926	1,000	100.	100,000								
				(	50			Mar. 12 1931	400	100	40,000							
				(2/24/30															
Officers																			
Date	Name	Title	Service of Process on																
		President																	
		Vice-President																	
		Secretary																	
		Treasurer																	
		Auditor																	
Annual Exhibits																			
Years and Filing Numbers																			
1911	1912	1913	1914	1915	1916	1917	1918	1919	1920	1921	1922	1923	1924	1925	1926	1927	1928	1929	1930
															83	25	49	32	65
Years and Filing Numbers																			
1931	1932	1933	1934	1935	1936	1937	1938	1939	1940	1941	1942	1943	1944	1945	1946	1947	1948	1949	1950
Nature of Business																			
Place of Principal Office																			
Honolulu																			
Name										Filing No.									
E. E. BLACK LIMITED										1831									

Formerly E. J. Lord Limited, name changed Feb'y 24, 1930
to

[Endorsed]: No. 2052. Filed February 1, 1932 at
11:40 o'clock A. M. Robert Parker, Jr., Clerk
Supreme Court.

[273]

Mr. WRENN: I would like to offer as one exhibit at this time Exhibit 6, the annual corporation exhibit of E. J. Lord, Limited, for the year ending December 31, 1926.

(Document offered in evidence received [34] and marked: "Taxpayers' Exhibit 6A.")*

Mr. WRENN: The annual corporation exhibit of E. J. Lord, Limited, for the year ending December 31, 1927.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 6B.")*

Mr. WRENN: The corrected annual corporation exhibit of E. J. Lord, Limited, for the year ending December 31, 1927.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 6C.")*

Mr. WRENN: The annual corporation exhibit of E. J. Lord, Limited, for the year ending December 31, 1928.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 6D.")*

Mr. WRENN: The annual corporation exhibit of E. J. Lord, Limited, for the year ending December 31, 1929.

(Document offered in evidence received and marked "Taxpayers' Exhibit 6E.")*

Mr. WRENN: And annual corporation exhibit of E. E. Black, Limited, for the year ending December 31, 1930.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 6F.")*

*Omitted from printed record on stipulation by counsel.

Mr. WRENN: May we leave these until the conclusion of the case with the privilege of withdrawing them?

Mr. NYE: We will have to have them back.

Mr. WRENN: We will substitute copies.

Mr. KAY: May it please the Board, unless stipulated to by counsel that Mr. Adams may later consider this case by reading the evidence appearing in the transcript, it is going to be difficult for us to proceed. I suggest we wait until Mr. Adams appears. It is hardly proper for this Board to proceed and hear this evidence in the absence of one of the members. It would be hardly proper for the member to later consider the case, not hearing all the evidence.

Mr. WRENN: We are perfectly willing to stipulate that Mr. Adams can read the transcript and go ahead as if he were here. We will raise no objection to the fact that he is not here.

E. C. PETERS

was duly called and sworn as a witness for the Taxpayer, and testified as follows:

Direct Examination by Hearon L. Wrenn, Esq.

Q. Will you state your name, please?

A. E. C. Peters.

Q. Judge Peters, you are a member of the bar of all the Courts of the Territory of Hawaii?

A. Yes.

(Testimony of E. C. Peters.)

Q. And former Chief Justice of the Supreme Court of the Territory of Hawaii?

A. I was.

Q. And in 1929 were you the attorney for E. J. Lord, [35] Limited?

A. I was as under a regular retainer of E. J. Lord, Limited during the period, during the entire year of 1929.

Q. As a matter of fact you were the regular attorney under retainer of E. J. Lord, Limited, from its incorporation in 1926 to 1929?

A. I would not say exactly as to that, Mr. Wrenn, but I think it covered a period of at least two years.

Q. In 1929 were you consulted by Messrs. Black and Lord in regards to the redemption of capital stock of E. J. Lord, Limited, by the corporation?

A. I was. I was consulted by Mr. E. J. Lord, as president of E. J. Lord, Limited, and by Mr. Black, as one of its officers, and both of them comprising all of the stockholders with the exception of three, I think, each of whom held one share for the purposes of qualification in acting upon their directorate, at my office, touching the redemption of the stock then held and owned by Mr. Lord.

Q. Mr. Lord at that time held six hundred shares, didn't he, of the capital stock of E. J. Lord, Limited?

A. I think that is the correct figure.

Q. And Mr. Black four hundred shares?

A. Yes.

(Testimony of E. C. Peters.)

Q. Can you give us in detail just what E. J. Lord, Limited, was desirous of doing at that time in [36] regard to the stock which was owned by Mr. E. J. Lord?

A. Yes. The question first arose in the early part of December. Mr. Lord at that time was having domestic difficulties, his health was not too good, and Mr. Black was apprehensive of complications that might arise in the event of Mr. Lord's demise, and he came to the office and saw me about the proposition of the corporation acquiring and redeeming the stock then owned by Mr. Lord. I told Mr. Black that that was a matter he would have to take up personally with Mr. Lord; that, as controlling stockholders of the corporation, they would have to get together, and just as soon as they came to a mutual understanding as to the price on the one hand that Lord would expect to receive for his stock, and what the corporation on the other hand was willing to pay him for the redemption of his stock, that after they had arrived at a mutual understanding they were both to come to the office and discuss the situation. That was, as I say, along about the early part of December, and along about the 11th of December Mr. Lord and Mr. Black came to the office. The question then arose as to the *modus operandi*. I asked Mr. Black what the intentions of E. J. Lord, Limited, were, and particularly of himself, what they would be in the event of the elimination of Mr. Lord as a stockholder in the company. He told me he wanted it [37] arranged

(Testimony of E. C. Peters.)

so that the company acquire Mr. Lord's stock, and that just as soon as that stock was acquired and the consideration as ascertained paid to Mr. Lord, that the stock would be retired, and that the remaining shares of stock held by himself would represent the entire capital stock of the company. I asked him if he understood that as far as the situation was concerned that there were two methods of carrying forth what his and the company's desires were? One was the purchase of Mr. Lord's stock and its retention in the treasury as treasury stock and its subsequent disposition to others, if he desired to have increased capital in the corporation. The other method was to acquire the stock from Mr. Lord and retire that stock and reduce the capital of the corporation so that it was consistent with the value of the remaining stock. He told me that the latter method of the retirement of the stock and reduction of the capital stock was what he wanted, and on that basis I looked up what authorities were available to see just exactly what steps should be taken. The conference of December 11th resulted in an agreement between the corporation, on the one hand, and Mr. Lord on the other, that Lord was to receive what he had originally put into the corporation by way of contribution on the original organization, and that he was to also receive the undivided profits, [38] which, with the capitalization would represent the net worth of the business, and that net worth was to be computed as of the close of the year 1929, De-

(Testimony of E. C. Peters.)

cember 31st. The necessity of awaiting the closing of the books and the audit was apparent, and the net worth was adopted as the basis of computation due to the statement that Mr. Lord made at that time that certain articles of plant, which under the formula provided by the Engineers' Association, American Engineers' Association, that according to good bookkeeping had been wiped off the inventory, that there were certain articles of machinery and equipment that had thus been wiped off, and he wanted to be sure that the net worth as ascertained at the end of the year included every article of plant. So, whereas the plant might show one value upon an appraisement and further investigation that value would have to be increased, so they were not closing on the basis of an actual net worth book value, but they were closing on a net worth value on which all the figures of the auditors and bookkeepers would be accepted, with the exception of inventory of plant. One of the items of consideration was the existing contracts E. J. Lord, Limited, at that time—

Mr. KAY: I have no objection to Judge Peters stating that these men, to-wit Mr. Lord and Mr. Black, approached him to draw up a contract, and he drew [39] up a contract pursuant to their request, but for Mr. Peters to testify as to what their intentions were and what they told him and all the surrounding facts of this transaction is to my mind clearly hearsay and immaterial as far as this witness is concerned and inadmissible. The documents

(Testimony of E. C. Peters.)

speak for themselves, and as far as the documents are concerned, if they are properly identified, there is no objection to their admission, but if Judge Peters' testimony is going to be a substitution for what Mr. Black and Mr. Lord would testify to, we would have to object, because we are entitled to our right of cross-examination of what their intentions were. We object to this line of testimony.

Mr. WRENN: I take it what the Board is after in this is to get down to really what happened at that time, at the time this transaction transpired, and to get the real intention of the parties. The testimony that Judge Peters is about to give, from a legal viewpoint, is entitled to be admitted, because it is part of the *res gestae*, things that occurred at the time the contract was entered into, and has a material bearing on the issue which is now being tried before the Board; but it seems to me, even though that is true as to a technical matter, part of the *res gestae*, the Board is interested in getting what was in the minds of the parties and how the attorneys proceeded to carry [40] these things out. I think it is clearly admissible on those grounds.

The CHAIRMAN: Objection overruled.

Mr. KAY: May we have our objection to this whole line of testimony, and exception to the ruling of the Board?

The CHAIRMAN: Certainly.

A. (Continuing.) As I was saying, the closing items for the year 1929 would not disclose Mr.

(Testimony of E. C. Peters.)

Lord's interest in certain contracts which E. J. Lord, Limited, had at that time, and which were incomplete, it being the accepted method and the particular method in the bookkeeping of E. J. Lord, Limited, as disclosed by Mr. Buchholtz, that whatever profits in any contract might accrue to the contractor, that the profits were not computed and entered in the books of the company until the final acceptance of the contract by the owner. All of these were public contracts and awaited acceptance by the authoritative officers of the Government,—so that the proposition was that Mr. Lord claimed that he was entitled to a percentage of profits that might accrue from those contracts, and hence, in addition to the consideration of sixty per cent. of the net worth of the business at the close of 1929, Mr. Lord said he was entitled to and Mr. Black on behalf of the company said it was willing to pay sixty per cent. of the profits [41] of certain outstanding contracts, when and as those contracts were completed and the profits computed; likewise as to any losses. So that on the 11th of December, 1929, at the time that this consultation was had with Mr. Lord and Mr. Black, it was agreed primarily that Mr. Lord was to receive sixty per cent. of the net worth of the business as it was disclosed at the end of the year and sixty per cent. of the profits that might accrue upon these contracts, a list of which Mr. Buchholtz was to furnish. I have a notation of the consultation. I have a sys-

(Testimony of E. C. Peters.)

tem in my office of making daily charge sheets, so that we can find out afterwards what we have done or refresh our memory as to what is done and make charges. Of course it doesn't mean we always get paid for that work, but we make the charges, nevertheless, and I have a memorandum as to that day, which I have picked out of my finished filed in the matter of the redemption of this stock for that day.

Q. Have you any objection to having this memo admitted in evidence?

A. Not at all, if it be of any value.

Mr. WRENN: We offer it in evidence.

Mr. KAY: We object to this. Mr. Lord and Mr. Black are proper witnesses on this matter.

Mr. WALSH: This is of no value to the Board.

Mr. WRENN: We submit it is of very material value [42] to the Board to show conclusively that on the 11th day of December, 1929, the corporation on one side, and Mr. Lord on the other side, had in mind the question of the corporation redeeming the capital stock he had at that time. This is an entry made contemporaneous with the discussions that took place at that time with Judge Peters, counsel for the corporation, indicating quite clearly that what was in the minds of the parties was a redemption of the stock of the corporation.

Mr. WALSH: Judge Peters has testified to that. This is merely a written confirmation of what occurred in his office. The real confirmation comes from the parties concerned.

(Testimony of E. C. Peters.)

Mr. WRENN: May we have this marked for identification?

(Document offered to be marked for identification received and marked: "Taxpayers' Exhibit 7 for identification.")*

Q. That entry was made by you on that day?

A. That entry was made by me on that day.

Q. And it was made at the close of the consultations which you had with Mr. Lord and Mr. Black on that day?

A. Yes. I want it distinctly understood that in this conference of December 11, 1929, I was acting for E. J. Lord, Limited. This entire work was done and charged against E. J. Lord, Limited, and paid for [43] by E. J. Lord, Limited, and prior to coming on the stand this morning Mr. Black, the president of E. E. Black, Limited, and successor of E. J. Lord, Limited, requested of me that I testify in this matter, and hence I am not violating any professional privilege. I think that was all that occurred on that day. There was, of course, considerable discussion. The memoranda will show that period of time in which Mr. Lord and Mr. Black were in my office. Mr. Lord and Mr. Black came back to the office the following day, the 12th of December, and it seems that the necessity of immediately drawing up this agreement had arisen. Mr. Black stated that Mr. Lord was contemplating going to San Francisco, and that he would like very

*Omitted from printed record on stipulation by counsel.

(Testimony of E. C. Peters.)

much to have an option drawn up reflecting the conversation and agreement of the day previous, and a contract was drawn up. Mr. MacComiskey was called into consultation on the question of Federal taxes. Mr. Buchholtz was called into consultation relative to the outstanding contracts and their identity and was asked to secure immediately the definite details of those contracts; and that was about ten o'clock in the morning when Mr. Lord and Mr. Black called. I was requested to have the contract ready by two o'clock. They came back again at two o'clock and there was some delay and finally, along about half-past four, the contract [44] was in final form. We had to wait for Mr. Buchholtz, as an officer of the company, to come down and sign it, and finally, as a notary, we secured Miss Sylvia Bryant, and the contract was concluded that afternoon. I made memoranda of what happened on that day. I won't say they are entirely complete, but they were sufficient for my purposes. (Witness produces papers.)

Mr. WRENN: I offer these three daily charge sheet memos dated December 12, 1929, in evidence.

Mr. KAY: Same objection as stated as to the other slip, and on the further ground evidently these slips are being introduced for the purpose of corroborating a matter that has not yet been presented to the Board. In other words, Judge Peters has been called out of order, if Mr. Wrenn intends to put on Mr. Black and Mr. Lord, and at that time

(Testimony of E. C. Peters.)

we will question them as to these conferences and what took place there,—I can see the materiality of Judge Peters' evidence, if it is material to the evidence in this case. Meanwhile, it seems to me this evidence is clearly hearsay and not admissible.

Mr. WRENN: This evidence is not out of order. It is perfectly in order, and it is perfectly competent, relevant and very important testimony,—perhaps the most important testimony we could offer; more important than relying upon the recollection [45] of this witness, and it certainly of course does corroborate what Judge Peters has been testifying to and indicates quite clearly the intention of the parties.

The CHAIRMAN: Objection sustained.

Mr. WRENN: I offer the three of them, then, as an exhibit for identification.

(Documents offered for identification received and marked: "Taxpayers' Exhibit 8 for identification.")*

Q. Have you with you here the final original contract that was prepared by you at the request of E. J. Lord, Limited, and Mr. E. J. Lord individually?

A. I have.

Q. Are you familiar with the handwriting of Mr. E. J. Lord?

A. I am. I have seen him write numerous times.

*Omitted from printed record on stipulation by counsel.

(Testimony of E. C. Peters.)

Q. In your opinion is the signature on that contract the signature of E. J. Lord?

A. It is. I saw him sign it and saw Mr. Buchholtz sign on behalf of E. J. Lord, Limited, and saw them acknowledge their signatures before Sylvia Bryant.

Mr. WRENN: We offer the copy of the agreement dated December 13, 1929, between E. J. Lord of Honolulu and E. J. Lord, Limited, in evidence as Exhibit 7.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 7.") [46]

TAXPAYERS' EXHIBIT 9.

8 pages

(9)

FILED February 1, 1932

AT 11:40 o'clock A. M.

(s) ROBERT PARKER, JR.

Clerk Supreme Court.

THIS INDENTURE OF AGREEMENT made and entered into this 13th day of December, A. D. 1929 by and between E. J. LORD, of Honolulu, City and County of Honolulu, Territory of Hawaii, party of the first part, and E. J. LORD, LIMITED, an Hawaiian corporation having its principal place of business in said Honolulu, party of the second part,

WHEREAS the party of the first part is the owner of, and appears upon the stock books of the

(Testimony of E. C. Peters.)

party of the second part as the owner of six hundred (600) shares of the capital stock of the party of the second part, evidenced by certificates of stock of said party of the second part numbered 7, 8 and 9 for 310, 200 and 90 shares respectively, now outstanding in the name of the party of the first part; and

WHEREAS the party of the second part desires to redeem said shares of stock; and

WHEREAS the party of the first part is willing to accept as consideration for the sale of said stock to the party of the second part, and the said party of the second part is willing to pay to the said party of the first part for the redemption of said stock, a sum of money equal to sixty per cent (60%) of the net worth of the party of the second part as of December 31, 1929 and a sum of money equal to sixty per cent (60%) of the net profits yet to accrue to the party of the second part by its completion of the respective works contemplated by certain executory contracts to which the said party of the second part is a party, remaining uncompleted, and the further sum of money equal to forty per cent (40%) of the amount to which the party of the first part may become [274] liable to the United States of America and/or the Territory of Hawaii for income taxes upon income accrued and/or to accrue to him by reason of and resulting from the exercise by the party of the second part of the option hereby granted and the

(Testimony of E. C. Peters.)

consummation of the sale of said six hundred (600) shares of the capital stock of said party of the second part; and

WHEREAS the net worth of the party of the second part cannot be determined until the books of the party of the second part have been closed for the year 1929 and an audit made thereof; and

WHEREAS the following enumerated contracts, to which the party of the second part is a party, remain uncompleted: Territory of Hawaii and City and County of Honolulu by Honolulu Sewer and Water Commission with E. J. Lord, Ltd., First section of Manoa-Kaimuki interceptor, dated July 16, 1928; City and County of Honolulu with E. J. Lord, Ltd., Improvement District Number 29, St. Louis Heights, dated August 20, 1929; Lyman H. Bigelow, Territorial Highway Engineer with E. J. Lord, Ltd., Kalanianaʻole Highway, F. A. Project No. 6A, Job #4034, dated (May 14, 1928) May 24, 1929; Territory of Hawaii by Board of Harbor Commissioners with E. J. Lord, Ltd., wharf and freight shed Pier #1 Nawiliwili, dated August 7, 1929; Territory of Hawaii by Board of Harbor Commissioner and E. J. Lord Ltd., Pier #2 Kapa-lama Basin, dated —————:

NOW, THEREFORE, THESE PRESENTS WITNESSETH:

That the party of the first part, in consideration of the sum of One Dollar (\$1.00) to him in hand paid by the party of the second part, the receipt

(Testimony of E. C. Peters.)

whereof is hereby [275] acknowledged, and the covenants and agreements of the party of the second part hereinafter contained, on its part to be kept and performed, does hereby and by these presents:

1. Give and grant to the party of the second part an option, irrevocable within the time for acceptance herein limited, to purchase free from encumbrances the said six hundred (600) shares of the capital stock of the party of the second part so owned by him and so evidenced and so outstanding as aforesaid for the consideration hereinafter set forth.

2. Assign and deliver unto the said party of the second part six hundred (600) shares of the capital stock of the party of the second part so owned, evidence and outstanding as aforesaid, duly endorsed by him on the back thereof to the order of the party of the second part by way of pledge to secure the performance by him of the covenants and agreements hereof on his part to be kept and performed, and does constitute and appoint the said party of the second part his true and lawful attorney for him and in his name and stead, upon the exercise of the option hereby granted by the party of the second part, to cause said six hundred (600) shares of the capital stock of the party of the second part to be redeemed by the said party of the second part and the same to be recorded on the proper books of the party of the second part.

And in consideration of the covenants and agree-

(Testimony of E. C. Peters.)

ments of the party of the first part hereinbefore contained and the sum of One Dollar (\$1.00) in hand paid by the party of the first part to the party of the second part, the receipt whereof is hereby acknowledged, the party of the second part [276] does hereby and by these presents covenants and agrees by and with the party of the first part as follows:

1. That it will, as soon as may be, at its own proper cost, cause its books to be closed as of December 31, 1929 and cause the same to be admitted by a competent auditor or competent auditors.

2. That it will, as soon as may be, at its own proper cost, fully perform and complete the work respectively contemplated by the pending contracts hereinbefore enumerated, to which it is a party, in a workmanlike and economical manner, and will, as soon as may be, reduce to possession all moneys, bonds or other consideration accruing and payable or deliverable to it thereunder.

3. That it will keep and have open for the inspection of the party of the first part at its place of business full and complete books of account of the receipts and disbursements respectively made and received by it on account of said pending contracts.

4. That said party of the second part, upon the exercise of the option by it to it hereby granted, will, as soon as may be, cause its articles of association to be amended so that its name does not con-

tain the name "E. J. Lord" or any part of said name, or contain any words similar to said name "E. J. Lord" or any part thereof.

And the parties hereto, in consideration of their status hereunder, mutually covenant and agree;

1. That the option hereby given shall be open for acceptance up to, but not after the 28th day of February, 1930, and may be accepted by letter delivered to the party of the first part or mailed, postage prepaid and registered, addressed [277] to the party of the first part at his residence at Dowsett Highlands, Honolulu.

2. That the purchase price of the said stock of the party of the second part shall be a sum of money equal to sixty per cent (60%) of the net worth of the party of the second part as of December 31, 1929 and a sum of money equal to sixty per cent (60%) of the net profits yet to accrue to the party of the second part by its completion of the respective works contemplated by said pending contracts, to which it is a party, now remaining uncompleted, and the further sum of money equal to forty per cent (40%) of the amount to which the party of the first part may become liable to the United States of America and/or the Territory of Hawaii for income taxes upon income accrued and to accrue to him by reason of and resulting from the exercise by the party of the second part of the option hereby granted and the consummation of the sale of said six hundred (600) shares of the capital stock of the party of the second part. That

(Testimony of E. C. Peters.)

such purchase price shall be paid to the party of the first part at the time and in manner following, that is to say: the sum of money equal to sixty per cent (60%) of the net worth of the party of the second part as of December 31, 1929 forthwith upon the exercise by the party of the second part of the option hereby granted to it. In the event that the amount so payable exceeds the sum of Two Hundred Fifty Thousand Dollars (\$250,000.00), the amount of the excess over that sum may be retained by the party of the second part until and paid by it to the party of the first part upon the completion of the St. Louis Heights contract and the receipt by it of the full consideration for the performance thereof; [278] the sum of money equal to sixty per cent (60%) of the net profits yet to accrue from each of the foregoing enumerated uncompleted contracts when completed and the moneys, bonds or other consideration accrued and payable or deliverable to the party of the second part thereunder, reduced to possession, and the sum of money equal to forty per cent (40%) of the income tax to which the party of the first part may become liable to the United States of America and/or the Territory of Hawaii for income taxes upon income accrued or to accrue to him by reason of and resulting from the exercise by the party of the second part of the option hereby granted and the consummation of the sale of said six hundred (600) shares of the capital stock of the party of the second part, forthwith upon assessment.

(Testimony of E. C. Peters.)

3. That if any dispute or difference shall arise and exist between the parties hereto in respect to any provision hereof, said dispute and cause of difference shall be referred and submitted to the arbitration and determination of three persons, two of whom shall be accountants and one of whom shall be an engineer; that the parties hereto now nominate and appoint as such arbitrators, H. Douglas Young, an accountant, J. K. Lamberton, an accountant, and Fred E. Harvey, an engineer. In case any of such arbitrators shall die or refuse or become incapable to act as arbitrator, substitution shall be made from the following named alternates, such substitute to be of the same profession as the arbitrator for whom he is substituted. The parties hereby nominate as alternates, Fred G. Pearson, an accountant, L. N. MacComiskey, an accountant, and J. L. Young, an engineer. Any substitute arbitrator shall have the same powers and authority as the arbitrator first appointed hereunder, for whom he is substituted, would have had if he had acted on *con-* [279] *be* final as between the parties hereto and shall in all respects be kept and faithfully observed by them and neither party hereto shall bring or prosecute any action against the other nor against the arbitrators nor any of them concerning the matter in difference or any of them concerned in any reference. The cost of any arbitration shall be borne equally by the parties hereto.

(Testimony of E. C. Peters.)

4. That time is of the essence hereof.

5. That the term “party of the first part” wherever employed herein, when agreeable to the context, shall be understood to mean and include the party of the first part and his executors, administrators and assigns, and that the term “party of the second part” shall be understood to mean and include the party of the second part, its successors and assigns.

IN WITNESS WHEREOF, the party of the first part has set his hand and seal and the party of the second part has caused its name to be hereunto subscribed and its corporate seal affixed hereto and to another instrument of like date and tenor by its proper officers thereunto duly authorized, the day and year first above written.

[Seal] E. J. Lord.
E. J. LORD, LIMITED.

[Seal] By E. E. Black,
Vice-President.
Geo. Buchholtz,
Treasurer.

[280]

City and County of Honolulu
Territory of Hawaii—ss.

On this 13th day of December, A. D. 1929, before me personally appeared E. J. LORD, to me known to be the person described in and who executed the

(Testimony of E. C. Peters.)

foregoing instrument and acknowledged that he executed the same as his free act and deed.

[Seal]

SYLVIA LESLIE BRYANT,
Notary Public, First Judicial Circuit,
Territory of Hawaii.

City and County of Honolulu
Territory of Hawaii—ss.

On this 13th day of December, A. D. 1929, before me appeared E. E. BLACK and GEORGE BUCHHOLTZ, to me personally known, who being by me duly sworn, did say that they are the Vice-President and Treasurer respectively of E. J. LORD, LIMITED, and that the seal affixed to the foregoing instrument is the corporate seal of said corporation and that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors, and the said E. E. Black and George Buchholtz acknowledged said instrument to be the free act and deed of said corporation.

[Seal]

SYLVIA LESLIE BRYANT,
Notary Public, First Judicial Circuit,
Territory of Hawaii. [281]

Q. After the execution of this agreement did you have any further conferences as to the redemption of Mr. Lord's stock by E. J. Lord, Limited, with Mr. Lord and Mr. Black?

A. I did.

(Testimony of E. C. Peters.)

Q. When was the next conference, as your records show?

A. The next conference I had with Mr. Lord and Mr. Black was on the day following.

Q. What was that conference about?

A. I have no,—I haven't any particularly clear recollection of what occurred on the 13th of December. I have a notation in the handwriting of my stenographer, and I have my own handwriting which I must have made after their departure, "E. J. Lord and Mr. Russell called re option Lord."

Mr. WALSH: You mean the 14th, don't you?

A. Yes, that's true. The memoranda on the 12th that I speak of do not refer to the details of the calling of Mr. Lord and Mr. Black on the 13th, when they called in the morning and the contract was drafted, and they came in in the afternoon and executed it. The details of the 12th were further discussions, somewhat along the same lines as the 11th. I remember that Mr. Russell came in with certain grammatical suggestions relative to the contract and they were accepted and the contract was executed in its final form such as you have [47] offered and admitted in evidence.

Q. This Mr. Russell you refer to is Mr. Russell of Davies & Company?

A. Yes, Mr. Russell of Davies & Company.

Q. And he was consulted at the suggestion of Mr. Black to look over this contract?

A. Yes, Mr. Russell, as I understood from Mr. Black, was to assist E. J. Lord, Limited, in what-

(Testimony of E. C. Peters.)

ever financing was required, and I asked Mr. Black on the day we drafted the contract to go down and see Mr. Russell and show it to him, and, if he desired to consult with Mr. Edmondson, an attorney at law associated with Mr. Russell.

Q. The entries on this charge sheet of December 14, 1929, are in your handwriting?

A. Yes, and made by me at the time.

Mr. KAY: Same objection.

The CHAIRMAN: Objection sustained.

Mr. WRENN: I offer this to be marked for identification.

(Document offered to be marked for identification received and marked: "Taxpayers' Exhibit 10 for identification.")*

Q. When were you again consulted by either of these two gentlemen?

A. I was consulted from time to time, but they were mere details in the consummation of the agreement. For instance, in the latter part of December [48] the question arose over the auditors who had been employed for the purpose of ascertaining this net worth, the question arose as to what charges for depreciation on the one hand, or rental on the other, should be charged on plant that was devoted to the completion of these uncompleted contracts, and there was a consultation with Mr. Lord and there was consultation with Mr. Buchholtz and

*Omitted from printed record on stipulation by counsel.

(Testimony of E. C. Peters.)

Mr. Black and it finally resulted in a letter to Messrs. Young, Lambertson and Pearson as to how to handle that matter, and memorandum was made as of the 23d and 26th in that regard.

Mr. WRENN: We offer each of these memoranda.

Q. These memos are in your handwriting and made on these respective dates?

A. The words "Mr. Buchholtz" and "Mr. Black" are written by my stenographer. The way that occurs is the stenographer, when a person calls, makes an entry of the name and date and—

Q. The words here "Redemption of stock" are in your handwriting?

A. In my handwriting made at the time of the call, similarly as to the slip of December 23d.

Mr. WRENN: I offer in evidence slip of December 23, 1929.

Mr. KAY: Same objection.

The CHAIRMAN: Objection sustained. [49]

Mr. WRENN: Exception, and I offer it to be marked for identification.

(Document offered for identification received and marked: "Taxpayers' Exhibit 11 for identification.")*

Mr. WRENN: I offer in evidence memorandum of December 26, 1929.

Mr. KAY: Same objection.

The CHAIRMAN: Sustained.

*Omitted from printed record on stipulation by counsel.

(Testimony of E. C. Peters.)

Mr. WRENN: Exception, and I offer it for identification.

(Document offered for identification received and marked: "Taxpayers' Exhibit 12 for identification.")*

Mr. WRENN: Q. And the memo of December 27, 1929, the redemption of stock, E. J. Lord, that is in your handwriting?

A. Yes.

Mr. WRENN: I offer that in evidence.

Mr. KAY: Same objection.

The CHAIRMAN: Objection sustained.

Mr. WRENN: Exception, and I offer it for identification.

(Document offered for identification received and marked: "Taxpayer's Exhibit 13 for identification.")*

Q. Mr. Buchholtz at that time was treasurer of E. J. Lord, Limited?

A. He was, and was handling the retails of the [50] closing items. We were waiting upon Mr. Buchholtz to close the books, and particularly to get up an itemization of plant account. That seemed, in December and January, to be the burden of Mr. Lord's calls at the office, and Mr. Buchholtz. For instance, I have a notation in my handwriting, with the exception of the date and Mr. Buchholtz' name, On January 20th 1930, "Mr. Buchholtz called re valuation." It harped back to that original thought

*Omitted from printed record on stipulation by counsel.

(Testimony of E. C. Peters.)

of determining Mr. Lord's interest from a net worth value which actually reflected the true and not on any arbitrary net worth as reflected by the books, including this plant account, many articles of which it was pointed out by Mr. Lord had been used on contracts and the period of their life had lapsed, and for that reason they had been dropped from the plant account and Mr. Lord was anxious to receive every dollar of interest to which he was entitled in those portions of the plant, and that did not appear on the plant account of the books, and Mr. Buchholtz called on the 20th of January.

Q. Mr. Buchholtz was thoroughly familiar with the transactions and the corporation's desire to redeem the stock?

A. Mr. Buchholtz was thoroughly familiar with what was going on. The matter had been discussed between [51] himself and myself for the purpose of his having clearly in mind what was the arrangement between Mr. Lord and Mr. Black, so he could pursue his duties as treasurer of the corporation. Accordingly on the 23d of January Mr. Buchholtz called at the office again, on the 21st of January he having filed with me his first statement of what the books reflected upon the closing entries of the year 1929, and he told me at that time that there were still matters he had to get in, but it was in rough shape and we went over again the question of net worth. I have my memorandum, "Mr. Buchholtz in re statement of net worth, December 21, 1929," and that matter continued until I had a

(Testimony of E. C. Peters.)

conference with Mr. Black. I told him Mr. Lord was dissatisfied with the inventory of plant; that he was dissatisfied with the valuation of plant, and that under all the circumstances I would advise that some independent person be called in in regard to the value of the plant. Mr. Black demurred to that. He said he thought Mr. Lord was over captious. He felt that the book value of the plant as it was was in excess of its actual value, but he said if Mr. Lord wanted to question that valuation it was all right with him, and Mr. Fred Williams was employed,—formerly of Aiea, Waipahu and Waialua plantation, and he proceeded with an inventory of plant and report upon it was finally filed with me and called to the attention of Mr. [52] Black and Mr. Lord on the 3d of April 1930; so that from the time of the closing of the books on December 31st and until that time, April of 1930, the question of valuation of plant was still a matter of discussion. In the meantime I had drafted, pursuant to the contract a petition for amendment of the articles of association of E. J. Lord, Limited, changing the name to E. E. Black, Limited, and in that regard I should like to say that this matter of E. E. Black, Limited, came up for discussion in the first preliminary meetings. Mr. Black insisted that as long as this stock was to be retired, and he was practically to be the sole owner of the business, he wanted a change of name to E. E. Black, Limited, and Mr. Lord, on the other hand, felt that was proper and also felt that he perhaps might de-

(Testimony of E. C. Peters.)

sire to embark in business for himself and it was better that E. J. Lord, Limited, change its name.

(Recess)

Q. During the recess I brought to your attention a copy of a letter addressed to Young, Lambertson & Pearson dated December 30, 1929. Is that the letter you stated as having been drawn by you advising the auditors of the transaction?

A. It is. I have a carbon copy if Mr. Kay would like to look at it. This carbon copy in my folder which would be the same as the original. [53]

(Witness produces paper)

Mr. WRENN: I offer it in evidence as Exhibit 14.

Mr. KAY: That will carry our objection in mind we are objecting to all this line of testimony as to immateriality and incompetency.

The CHAIRMAN: Objection overruled.

(Document offered in evidence received and
Marked "Taxpayers' Exhibit 14.")

TAXPAYERS' EXHIBIT 14.

(14)

December 30, 1929

Young, Lambertson & Pearson

Honolulu, T. H.

Gentlemen:

In the Matter of the Redemption Contract
between E. J. Lord, Ltd. and E. J. Lord,
dated December 13, 1929.

Mr. Buchholtz, our treasurer, has been instructed to charge each job in which Mr. Lord has an inter-

(Testimony of E. C. Peters.)

est, subject to the above marginal contract, with the value of the use of plant belonging to the company in accordance with the rates contained in the column entitled "Expense Per Working Month Per Cent" in the "Construction Equipment Schedule" found on page three of the publication of the Associated General Contractors of America Inc., 1038 Munsey Building, Washington, D. C., copyrighted 1927, entitled "Construction Equipment, a Report on Current Practice Pertaining to Construction Equipment, Including an Equipment Schedule, a Rental Agreement, Equipment Record and other Forms."

Respectfully yours,

E. J. LORD, LTD.

By—(Sgd.) E. E. BLACK.

By—(Sgd.) E. J. LORD. [282]

Q. I call your attention to a receipt dated February 15, 1930. Did you prepare this receipt?

A. Yes. Mr. Buchholtz called at the office and had a rough draft of receipt that he had prepared which contained the same figures and notes and bonds as contained in the receipt as finally drafted, and after a discussion of the matter I drew this receipt for him to sign,—to get Mr. Lord's signature to it, with certain instructions that he should advise Mr. Lord in respect to. The receipt afterwards I saw again with Mr. Lord's signature. I didn't see Mr. Lord sign this receipt, but that is his signature.

(Testimony of E. C. Peters.)

Mr. WRENN: I offer the receipt in evidence as Exhibit 15.

Mr. KAY: That carries our same objection we have interposed here to the whole line.

Mr. WRENN: That is the receipt showing payment by E. J. Lord, Limited, to E. J. Lord of the first installment under the contract.

The CHAIRMAN: Objection overruled. [54]

(Document offered in evidence received and marked: "Taxpayers' Exhibit 15.")

TAXPAYERS' EXHIBIT 15.

pages 1-2 (15)

Honolulu, Hawaii, February 15, 1930.

E. J. Lord, Limited having duly accepted the option granted by me to it by the indenture of agreement between us dated December 13, 1929, and the sum of Two Hundred Seventy-three Thousand Eight Hundred Fifty-five Dollars and Thirty-six cents (\$273,855.36) having been found to be sixty (60%) of the net worth of E. J. Lord, Limited as of December 31, 1929;

I hereby accept in lieu of cash and acknowledge receipt from E. J. Lord, Limited in payment of the sum of Two Hundred Fifty Thousand Dollars (\$250,000.00) on account of the purchase price of the six hundred (600) shares of the capital stock of E. J. Lord, Limited, the subject of said indenture, the following enumerated notes, bonds and cash:

(Testimony of E. C. Peters.)

Note Honolulu Iron Works @ 5½% \$ 50,000.00

Due 4/15/30

Interest from 1/1/30 payable direct to
E. J. LordNote Hawaiian Trust Co. @ 6½% \$ 50,000.00
payable on demandInterest from 1/1/30 payable direct to
E. J. LordBonds: St. Louis Hghts. Impr. Bonds 119,000.00
@ 5% Tax free
Coupons 2-18 attached from 2/15/30
(Interest see below)Bonds: Lihue Plant. Co. Bonds @ 5½% 15,000.00
Coupons 6-20 attached from 2/15/30
(Interest see below)Bonds: Seattle Lighting Co. Bonds 15,000.00
@ 5%
Coupons 41-80 attached from 10/1/29
(Interest see below)

Check for Balance 1,000.00

\$250,000.00

E. C. PETERS

Attorney at Law

Alexander & Baldwin Bldg.

Honolulu, Hawaii

(Testimony of E. C. Peters.)

I also hereby acknowledge the receipt from E. J. Lord, Limited of the sum of Six Hundred Fifty-six Dollars and Twenty-five Cents (\$656.25) interest on said bonds from January 1, 1930 to date in lieu of interest coupons covering said period computed as follows:

Interest payable to E. J. Lord	\$743.75
--------------------------------	----------

St. Louis Hghts. 1/1/30 to 2/15/30	
------------------------------------	--

11½ months	
------------	--

Interest payable to E. J. Lord	68.75
--------------------------------	-------

Lihue Pl. Co. 1/1/30 to 2/1/30	
--------------------------------	--

1 month	
---------	--

	\$812.50
--	----------

Less: Interest accrued	156.25
------------------------	--------

Seattle Lightg. Co. 10/1/29 to	
--------------------------------	--

1/1/30, 3 months	
------------------	--

	\$656.25
--	----------

(Sgd.) E. J. LORD.

E. C. PETERS

Attorney at Law

Alexander & Baldwin Bldg.

Honolulu, Hawaii

Receipt of Settlement with E. J. Lord \$250,000.00
2/15/30. [284]

(Testimony of E. C. Peters.)

Q. Just prior to the recess you spoke of handling for E. J. Lord, Limited, the matter of change of name to E. E. Black, Limited?

A. Yes. I drew a petition for the amendment of the articles of association of E. J. Lord, Limited. I drew up the minutes for the meeting of stockholders of E. J. Lord, Limited, and drafted a letter of instructions to Mr. Buchholtz as to what was to be done, and the meeting was held and petition signed and I finally sent it to the treasurer's office.

Q. I call your attention to Exhibit 2. Is that the petition you prepared at that time?

A. That is the petition. It is on my stationery.

Q. Why was it that you did not petition the treasurer of the Territory at that time for authority to reduce the stock?

A. The amount that was coming to Mr. Lord had as yet not been determined upon. The option required a certain payment to be made within a certain time and this payment, receipt for which is dated February 15, 1930, was the preliminary payment required by the option. If I might call to your attention that question of finances was a

discussion
matter of ~~discretion~~ on the 11th and 12th of December, and it was incorporated in the contract which the Board [55] will find on page 5. To pick up the thread,—“That such purchase price thereby paid to the party of the first part at the time and in manner following, that is to say an amount of

(Testimony of E. C. Peters.)

money equal to the net worth to the party of the second part as of December 31, 1929, forthwith upon the exercise by the party of the second part of the option hereby granted to it." The option was to December 31, 1930, and not sooner, but there was a letter written, I think, by the E. J. Lord, Limited, to Mr. Lord stating that the company exercised the option long prior to the time limitation. "In the event the amount so payable exceeds the sum of \$250,000. the amount of the excess over that sum may be retained by the party of the second part and paid by it to the party of the first part upon the completion of the St. Louis Heights Contract" etc., "and the receipt by it of the full consideration for the performance thereof."

The first payment of \$250,000. evidenced by that receipt was made by this provision of the contract, but the actual amount which was coming to Mr. Lord, and the amount by which the capital stock of E. J. Lord, Limited, would be reduced, could not be ascertained until these five or six incompleated contracts were completed, and then for the first time the books would take up the slack and make the closing entries, which would disclose the profits. [56]

Q. This reduction of the capital stock was made in the early part of 1931, after the final settlement with Mr. Lord?

A. Yes, it was. I might say in regard to that on the 27th of February, I think it was, 1930, E. J. Lord, Limited, for economical reasons sus-

(Testimony of E. C. Peters.)

pended the retainer which they, up to that time, had paid me, to take effect on the 28th of February, 1930. I thought Mr. Black might have waited until the end of March and not take advantage of just one day, but he closed it up on the 28th of February, and there were several inventory matters that spread down into the early part of 1931 for this reason. This question of plant became acrimonious as between Mr. Black and Mr. Lord, and I finally called Mr. Lord and Mr. Black in and said "Here, I have been representing E. J. Lord, Limited, in all these transactions. It has been satisfactory right straight along. Both of you gentlemen have been satisfied with my performances in the matter, but if you are going to get into a quarrel about this plant account you gentlemen will have to get somebody else." Black said he didn't want anybody else and wanted me to try to settle the thing up. I told him I couldn't do anything about it, I had represented Mr. Lord for years, I have the pleasure and privilege of his employment, and I didn't want to get in any [57] quarrel with the gentleman, and finally Mr. Lord came in and told me he had seen Mr. Thompson's office relative to it, and in August of 1930,— We had gone right along. They had this back and forth and some of it was hot and some of it was cold, but finally on the 6th of August I turned over the matter of the appraisement to Mr. Beebe. Then along towards the Fall,—in the meantime Mr. Lord was represented by the Hawaiian Trust Company as to his financial affairs, and Mr.

(Testimony of E. C. Peters.)

Black, as I understood it, had employed Judge Robertson's office. I could very easily see that there was going to be extended difficulties, and you must remember that during this time I was still representing Mr. Lord in his domestic affairs. There was a libel and cross-libel pending. I wanted to get his affairs settled up. I didn't want any more loose thread hanging, and I finally enlisted the services of the Hawaiian Trust Company by Mr. Peter McLean to get together with Mr. Lord and Mr. Black and the whole bunch decide that question of valuation. So finally, as my recollection serves me, in the early part of January or February the dove-of-peace was finally supreme, and this question was finally disposed of. Then the next thing,— Of course in the meantime I had ceased to be the attorney for E. J. Lord, Limited, and I noticed that within a very short time after the difficulties had been ironed [58] out, I noticed in the papers that E. J. Lord, Limited, applied to the Treasurer to reduce its capital stock, and that was the final step in the negotiations that began on December 11th in 1929.

Q. I call your attention to a receipt dated December 26, 1930, and the signature on that receipt?

A. Yes, I recognize both Mr. Buchholtz' and Mr. Lord's handwriting. I have seen Mr. Buchholtz sign his name upon numerous occasions.

Mr. WRENN: I offer receipt in evidence as Exhibit 16.

Mr. KAY: Same objection made as to all this line of testimony.

(Testimony of E. C. Peters.)

The CHAIRMAN: Objection overruled.

Mr. KAY: Exceptions.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 16.")

TAXPAYERS' EXHIBIT 16.

3 pages (16)

THIS AGREEMENT, made this 26th day of December, 1930, by and between E. E. BLACK, LIMITED (successor in name to E. J. LORD, LIMITED), an Hawaiian corporation, party of the first part, and E. J. LORD, of the City and County of Honolulu, Territory of Hawaii, party of the second part,

WITNESSETH:

That the party of the first part, in consideration of the transfer and delivery to it of six hundred (600) shares of the capital stock of said E. E. Black, Limited, by the party of the second part, does hereby assign, transfer and deliver to the party of the second part, the following bonds:

One hundred thirty-six (136) St. Louis Heights Improvement Bonds (par value \$500.00 each) with coupons attached from August 15, 1930,	\$ 68,000.00
Ten (10) Arkansas Light and Power Co. Bonds (par value \$1000.00 each) with coupons attached from October 1, 1930,	10,000.00
Ten (10) Alabama Power Co. Bonds (par value \$1000. each) with coupons attached from December 1, 1930,	10,000.00

(Testimony of E. C. Peters.)

Ten (10) Texas Power and Light Co. Bonds (par value \$1000. each) with coupons attached from November 1, 1930,	10,000.00
Nine (9) Emporium Capwell Corpora- tion Bonds (par value \$1000. each) with coupons attached from October 1, 1930,	9,000.00
	<hr/>
	\$107,000.00
And does hereby pay to said party of the second part in cash, the sum of	67,036.12
with interest thereon from July 31 to December 31, 1930, at the rate of two per cent (2%) monthly	670.36
Also interest accrued on the above men- tioned bonds since August 1, 1930, as follows:	
St. Louis Heights Improvement Bonds $\frac{1}{2}$ month at 5%	141.67
	<hr/>
(Forward)	\$174,848.15
	[285]
(Brought forward)	\$174,848.15
Arkansas Light & Power Co. 2 months at $5\frac{1}{2}\%$	91.66
Alabama Power Co. 4 months at 5%	166.67
Texas Power & Light Co. 3 months at 5%	125.00
Emporium Capwell Corporation, 2 months at $5\frac{1}{2}\%$	82.00
	<hr/>
	\$175,313.98

(Testimony of E. C. Peters.)

AND the party of the second part does hereby acknowledge receipt of the above mentioned bonds and cash aggregating the value of \$175,313.98, as full and final payment for said 600 shares of the capital stock of E. E. Black, Limited, and in complete settlement of the agreement made between said E. J. Lord and E. J. Lord, Limited, dated the 13th day of December, 1929, except as hereinbelow stated.

IT IS MUTUALLY UNDERSTOOD AND AGREED as follows:

1. That this settlement is based upon the assumption that the federal income tax upon the profits of E. E. Black, Limited, on the contracts mentioned in the said agreement of December 13, 1929, will amount to the sum of Ninety-five Thousand Five Hundred Sixty-seven and 93/100 Dollars (\$95,567.93), and that if upon the assessment of said taxes being made it shall develop that the amount thereof is more or less than said sum the parties hereto will make an adjustment whereby the one shall pay to the other such sum of money as will make up the difference.

E.E.B.Ltd.

G.B.

E.J.L.

2. And that the party of the first part will pay forty per cent (40%) of the federal and Territorial income tax which shall be assessed against the party of the second part by reason of and resulting [286] from the sale and transfer by him of said shares of E. E. Black, Limited.

(Testimony of E. C. Peters.)

IN WITNESS WHEREOF the said E. E. Black, Limited has caused its name and corporate seal to be set by its Treasurer thereunto duly authorized, and the said E. J. Lord has set his hand, hereunto and to another instrument of like date and tenor, the day and year first above written.

E. E. BLACK, LIMITED.

[Seal] By (Sgd.) GEO. BUCHHOLTZ,
Its Treasurer.

(Sgd.) E. J. LORD.

[Endorsed]: Final Settlement between E. E. Black, Ltd. and E. L. Lord 12/26/30. [287]

Q. Can you recall at this time any other discussions or transactions between the parties which throws any light on this situation?

A. I have a memorandum here in the same manner, same file, with my notations upon it, under date of February 17th, that "Mr. Lord and Mr. Black and Mr. Buchholtz called re valuation of plant. Buchholtz will get up list." I remember that. It was a question as to whether or not the plant account as contained in the books contained all the plant, [59] and I think Mr. Buchholtz was to get up a list of not only what was contained in the plant account but what might be in the yards or on any job. That was under date of February 17, 1930. I have a notation under date of February 25, 1930, "Conference with Mr. Lord and Mr.

(Testimony of E. C. Peters.)

Williams and conference re appraisement of plant of E. J. Lord, Limited." That is in relation to the employment of Mr. Williams. That is under the date of the 25th and Mr. Williams called in again the same day. The Hawaiian Trust was handling Mr. Lord's affairs in July. As early as July Peters got into the proposition,— Later on in the Fall of the year for the purpose of settlement, for I have a notation here that Mr. Buchholtz 'phoned me July 15th if certain bonds were to be delivered to me or to the Hawaiian Trust Company, and I told him to deliver them to the Hawaiian Trust. I have a distinct recollection of that, and find it on July 15th, 1930. The time it was turned over to Beebe is refreshed by a memorandum under date of August 5, 1930, "Conference with Lord and Beebe" and that hinges up with my evidence relative to Lord getting someone else to represent him independently, and I have on my slip it was conference with reference to retirement of stock.

Q. You made that on the date it indicated?

A. That is in my handwriting. [60]

Mr. WRENN: I offer this in evidence.

Mr. KAY: Same objection.

The CHAIRMAN: Objection sustained.

Mr. WRENN: Exception. I offer it to be marked for identification.

(Document offered to be marked for identification received and marked: "Taxpayers' Exhibit 17 for identification.")*

*Omitted from printed record on stipulation by counsel.

(Testimony of E. C. Peters.)

Mr. KAY: May it please the Board, we at this time move to strike the testimony of this witness on the ground that it is incompetent, irrelevant and immaterial, and the matters testified to are in the possession and knowledge of the officers of E. J. Lord & Company, to-wit, Mr. Black and Mr. Lord who are present in the court room. The evidence thus far adduced, whatever value it may have, is of a secondary nature, and the proper way, as I see it, to proceed, would be to call Mr. Black and Mr. Lord on these matters.

The CHAIRMAN: Motion denied.

Mr. KAY: Exception.

(Cross-examination waived.)

Mr. WRENN: I asked Mr. Glass if he would produce the original tax returns of E. J. Lord, Limited, for the calendar years 1926, 1927, 1928 and 1929. I offer in evidence the Territorial corporation income tax return for the 12 months preceding January 1, 1927, of E. J. Lord, Limited. [61]

(Document offered in evidence received and marked: "Taxpayers' Exhibit 18.")*

Mr. WRENN: I offer in evidence Territorial Corporation income tax return for the 12th months preceding January 1, 1928, of E. J. Lord, Limited.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 19.")*

*Omitted from printed record on stipulation by counsel.

(Testimony of E. C. Peters.)

Mr. WRENN: I offer in evidence corporation income tax return, Territory of Hawaii, E. J. Lord, Limited, for the 12 months preceding January 1, 1929.

(Document offered in evidence received and marked "Taxpayers' Exhibit 20.")*

Mr. WRENN: I offer in evidence corporation income tax return for the 12 months preceding January 1, 1930, Territory of Hawaii, E. J. Lord, Limited.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 21.")*

Mr. WRENN: And the corporation income tax return for the Territory of Hawaii for the 12 months preceding January 1, 1931, of E. E. Black, Limited.

(Document offered in evidence received and marked: "Taxpayers' Exhibit 22.")*

Mr. WRENN: I assume that the income tax return of E. J. Lord personally for the 12 months preceding January 1, 1931, is part of this record. And is the amended tax return of E. J. Lord for the twelve months preceding January 1, 1931, also a part of the record? [62]

*Omitted from printed record on stipulation by counsel.

GEORGE BUCHHOLTZ

was duly called and sworn as a witness for the Taxpayer, and testified as follows:

Direct Examination by Heaton L. Wrenn, Esq.

Q. What is your name?

A. George Buchholtz.

Q. You are the secretary and treasurer of E. J. Lord, Limited?

A. I am.

Q. And prior to the amendment of the articles of incorporation, changing the name to E. E. Black, Limited, you were treasurer of E. J. Lord, Limited?

A. I was.

Q. And you were the treasurer of E. J. Lord, Limited, from the time of its incorporation in 1926?

A. Yes, sir.

Q. Prior to the incorporation of E. J. Lord, Limited, you had been the bookkeeper for Mr. E. J. Lord, hadn't you?

A. Yes.

Q. And you compiled the figures which are the exhibit to the articles of incorporation showing the condition of affairs prior to incorporation and at the time of incorporation?

A. Yes.

Q. During the time you were treasurer of E. J. Lord, Limited, you had general supervision of the book accounts of the corporation, didn't you? [63]

A. Yes.

Q. And you still have of E. E. Black, Limited?

A. Yes.

(Testimony of George Buchholtz.)

Q. Have you the Territorial income tax receipts showing payment of Territorial income taxes of E. J. Lord, Limited, for the 12 months preceding January 1, 1927?

A. Yes

Mr. WRENN: I offer two receipts showing payments of taxes for first half and second half as one exhibit.

(Documents, consisting of six sheets, offered in evidence received and marked: "Taxpayer's Exhibit 23.")*

Mr. WRENN: I offer in evidence Territorial corporation income tax receipts for E. J. Lord, Limited, for the 12 months preceding January 1, 1928. These also show receipts for property taxes.

(Documents offered in evidence, consisting of eight sheets, received and marked: "Taxpayer's Exhibit 24.")*

Mr. WRENN: I offer in evidence two receipts showing payment of Territorial income tax receipts for the Territory for 12 months preceding January 1, 1929. These receipts also show payment of property taxes.

(Documents offered in evidence, consisting of nine sheets, received and marked: "Taxpayer's Exhibit 25.")* [64]

Mr. WRENN: I offer two receipts showing payment of Territorial income taxes of E. J. Lord,

*Omitted from printed record on stipulation by counsel.

(Testimony of George Buchholtz.)

Limited, for twelve months preceding January 1, 1930.

(Documents offered in evidence, consisting of four sheets, received and marked: "Taxpayer's Exhibit 26.")*

Mr. WRENN: I offer in evidence Territorial corporation income tax receipt for E. E. Black, Limited, for the twelve months preceding January 1, 1931, first half.

(Document offered in evidence, consisting of one sheet, received and marked: "Taxpayer's Exhibit 27.")*

Q. Has E. E. Black, Limited, paid the second half of its Territorial income tax?

A. Yes, it has.

Q. Have you the receipt?

A. I haven't it here. I don't know that I have it in the office. The reason for that is there was a dispute as to the property tax, I haven't it here. I can give you the date and the amount that was paid.

Q. Will you do that, please.

A. Dated November 13th.

Q. What is the amount of the taxes?

A. \$15,128.40.

Q. That is the latter part of the taxes for the [65] twelve months preceding January 1, 1931?

A. Yes.

*Omitted from printed record on stipulation by counsel.

(Testimony of George Buchholtz.)

Q. Do you recall in the latter part of 1929 a discussion between E. J. Lord, Limited, a corporation, on one side, and Mr. E. J. Lord, relative to the retirement of the capital stock in E. J. Lord, Limited?

A. I do.

Q. At that time Mr. E. J. Lord owned 600 shares of the capital stock of E. J. Lord, Limited?

A. Yes.

Q. And Mr. Black 400 shares?

A. Yes.

Q. And it was capitalized at \$100,000.?

A. Yes.

Q. What was the plan of the corporation at that time for redeeming the stock held by Mr. E. J. Lord?

A. Well, the company wanted to redeem that stock, but as our books show he closed off each share on the completed contract basis, and Mr. Lord was interested in all the uncompleted contracts which we had on hand on December 31, 1929. Some of those contracts were not completed until the latter part of the year. Therefore, there was only one possibility, as far as I could see; in fact, I took the thing up with Young, Lambertson & Pearson, our attorneys, how to handle the thing.

Q. Was the plan at that time to redeem as soon as [66] you had cash available the 600 shares of stock held by Mr. E. J. Lord?

A. Yes.

(Testimony of George Buchholtz.)

Q. And after that stock had been fully redeemed for the corporation to retire the stock by reduction of its capital and cancellation of the stock so redeemed from Mr. Lord?

A. I didn't get your question.

Q. Was it the plan of the corporation after it had fully redeemed Mr. Lord's stock, when cash became available, for that purpose, to then petition the Treasurer for reduction of its capital?

A. Yes, as soon as the deal was completed.

Q. To reduce its capital to forty thousand dollars?

A. To reduce its capital to forty thousand.

Q. And to cancel the stock redeemed from Mr. E. J. Lord?

A. Yes.

Q. And you took a prominent part in the negotiations, didn't you, between E. J. Lord, Limited, and Mr. E. J. Lord in regard to this transaction?

A. Yes.

Q. And, as I understand it, you compiled the figures that had to do with making up the contract of December 13th, 1929?

A. Yes.

Q. And also the compilation of the figures showing [67] the payment to Mr. E. J. Lord as shown by the receipts which have been admitted in evidence?

A. Yes.

(Testimony of George Buchholtz.)

Q. And, with this end in mind, you consulted freely with Mr. E. C. Peters, the attorney for the company?

A. Yes.

Q. Did you have charge of making the book-keeping entries to carry out this transaction?

A. I did.

Q. You have just stated that at the close of each year the books of the company were balanced, but only considering the contracts of the company actually completed at that time?

A. That's right.

Q. And you had a profit and loss account, did you?

A. Yes.

Q. And after the profit or loss was determined at the end of the year what was done with the credit balance, if any, which appeared in the profit and loss account?

A. To surplus account.

Q. From what amount were the dividends of E. J. Lord, Limited, paid?

A. From the surplus account.

Q. Have you had photostatic copies made of the surplus account as shown in the books of E. J. Lord, Limited, and subsequently on the books of E. E. Black, Limited?

A. They were made by Judge Peters. [68]

(Testimony of George Buchholtz.)

Q. I call your attention to what purports to be photostatic copies of the surplus accounts. Have you seen these sheets before?

A. Yes.

Q. Are they photostatic copies of the surplus account of E. J. Lord, Limited, and subsequently E. E. Black, Limited?

A. They are.

Mr. WRENN: I offer these two sheets in evidence.

Mr. KAY: We have no objection, subject to a later check by Mr. Glass.

(Documents offered in evidence, consisting of two papers, received and marked, respectively: "Taxpayer's Exhibit 28A" and "Taxpayer's Exhibit 28B.")

Sheet No. 1.

TAXPAYER'S EXHIBIT 28-A

Account No.

Rating Business	Credit Limit			Name SURPLUS ACCT. Address				
Date 1927	Items	Folio	✓ Debits	Balance	Credits ✓	Folio	Items	Date 1926
				5,818.51	5,818.51	J61	By E. J. Lord	Dec. 31 1927
Dec. 31	To P. & L. (Dividends)	J50	50,000.00		5,512.57	J51	“ Profit & Loss 1/1/27	Dec. 31
“ “	“ Reserve for Taxes	J50	15,600.00		84,469.99	“	“ “ “ “ 12/31/27	“ “
“ “	“ Balance		30,201.07					
			<u>95,801.07</u>		<u>95,801.07</u>			
				30,201.07	<u>30,201.07</u>		By Balance	
Dec. 31	To Sundry Exp. deferred	(J50)	15,057.03					
“ “	“ Balance		15,144.04					
			<u>30,201.07</u>		<u>30,201.07</u>			1928
				15,144.04	<u>15,144.04</u>		By Balance	Jan. 1
Dec. 31	“ Dividends pd. 1928	J20	100,000.00		2,634.47	J23	“ Reserve for Taxes	Dec. 31
“ “	“ Goodwill	“	23,535.13		283,015.18	J23	“ Profit & Loss	“ “
“ “	“ Balance		177,258.56			“		“ “
			<u>300,793.69</u>		<u>300,793.69</u>			1929
1929				177,258.56	<u>177,258.56</u>		By Balance	Jan. 1
Mar. 31	To Dividends	J36	30,000.00	147,258.56	125,697.94	J138	“ Profit & Loss	Dec. 31
April 30	“ “	J48	50,000.00	97,258.56				
May 31	“ “	J64	70,000.00	27,258.56				
	“ Balance		152,956.50					
			<u>302,956.50</u>		<u>302,956.50</u>			
1929				(152,956.50)	152,956.50		By Balance	1929 Dec. 31
Dec. 31	“ Life Ins. Deposits	J134	4,776.00					
“ “	“ Balance		148,180.50					
			<u>152,956.50</u>		<u>152,956.50</u>			
1930				148,180.50	148,180.50		By Balance	1930 Jan. 1
Aug. 31	To Dividends	J88	25,000.00	123,180.50				
Dec. 31	“ Balance		651,032.63		527,852.13	J145	“ Profit & Loss	Dec. 31
			<u>676,032.63</u>		<u>676,032.63</u>			

[Endorsed]: No. 2052. Filed February 1, 1932
at 11:40 o'clock A. M. Robert Parker, Jr., Clerk
Supreme Court. [298]

(Testimony of George Buchholtz.)

Account No.....		TAXPAYER'S EXHIBIT 28-B				Sheet No.....				
Name SURPLUS		Rating Business		Credit Limit						
Address										
Date 1931	Items	Folio	✓	Debits	Balance	Credits	✓	Folio	Items	Date 1931
Febr. 28	To Treasury Stock	J16		476,074.00	651,032.63	651,032.63			By Balance	Jan. 1
					174,958.63					
					234,958.63	60,000.00		J41	Capital Stock	May 31
					241,534.79	6,576.16		J45	Treasury Stock	" "

[Endorsed]: No. 2052. Filed February 1, 1932
at 11:40 o'clock A. M. Robert Parker, Jr., Clerk
Supreme Court. [299]

(Testimony of George Buchholtz.)

Mr. WRENN: May I explain for the benefit of the Board that the same surplus accounts were kept during the time of E. J. Lord, Limited, and E. E. Black, Limited?

A. None of the books were changed at all.

Mr. WALSH: You asked him if these were the surplus accounts of E. J. Lord, Limited, and E. E. Black, Limited?

Mr. KAY: I said and subsequently of E. E. Black, Limited. One is the continuation of the other. The name was the only thing that was changed.

Mr. WALSH: That is a whole lot.

Mr. PETERS: It is the same corporation, but the name [69] is changed.

Q. Does this account show the condition of the surplus account of E. J. Lord, Limited, from the time of its incorporation down to until the time E. E. Black, Limited, finally redeemed the outstanding shares of stock formerly held by Mr. Lord?

A. It does.

Q. And does the credit balance from the profit and loss account which has been transferred to this surplus account carry the profits of this corporation from all sources?

A. It does.

Q. Are the profits of this corporation, referring to E. J. Lord, Limited, subsequently known as E. E. Black, Limited, as shown on these surplus accounts,

(Testimony of George Buchholtz.)

—were they returned in the income tax returns of the corporation for the respective years 1926 to 1930, both inclusive?

A. They were.

Q. The profits which you have transferred to this account from your profit and loss account, and returned in your income tax returns, are profits on which Territorial income taxes were paid for the calendar years 1926, 1928, 1929 and 1930?

A. That's right.

Q. At the time the first payment to Mr. E. J. Lord was made by E. E. Black, Limited, under the option dated December 13, 1929, did you open an account [70] for E. J. Lord?

A. Settlement account.

Q. This photostatic sheet I call your attention to is a photostatic copy of the account kept in the books?

A. Correct.

Mr. WRENN: We offer this photostatic copy of the ledger account, E. J. Lord settlement account, as an exhibit.

Mr. KAY: No objection subject to the condition that Mr. Glass may check.

(Document offered in evidence received and marked: "Taxpayer's Exhibit 29.")

Q. At the time the first payment was made to Mr. E. J. Lord, February 30th, did you open an account known as "The Treasury account"?

A. "Treasury Stock Purchase Account."

Q. Is that the account in which you carried the stock of the corporation as redeemed from Mr. E. J. Lord?

A. Yes.

Q. This is a photostatic copy of the ledger account?

A. Correct.

Mr. WRENN: I offer in evidence photostatic copy of the Treasurer's stock purchase account.

Mr. KAY: Same understanding.

(Document offered in evidence received and marked: "Taxpayer's Exhibit 30.") [71]

(Testimony of George Buchholtz.)

Q. I call your attention to what purports to be a photostatic copy of the capital stock account. Is that aphotostatic copy of the capital stock account on the ledger of the corporation?

A. Yes, sir.

Mr. WRENN: I offer in evidence capital stock account from the ledger,—photostatic copy of the same.

(Document offered in evidence received and marked: "Taxpayer's Exhibit 31.")

(Testimony of George Buchholtz.)

Sheet No. 1.		TAXPAYER'S EXHIBIT 31				Account No.....				
Rating Business	Credit Limit	Name Address		CAPITAL STOCK						
Date	Items	Folio	✓	Debits	Balance	Credits	✓	Folio	Items	Date 1926
May 31 1931					100,000.00	100,000.00		J9	By Subscribed Stock	Aug. 1
	To Surplus	J40		60,000.00	40,000.00					

[Endorsed]: No. 2052. Filed February 1, 1932
at 11:40 o'clock A. M. Robert Parker, Jr., Clerk
Supreme Court. [302]

(Testimony of George Buchholtz.)

Q. I call to your attention a group purporting to be photostatic copies of journal accounts. I will ask you if these are the photostatic copies of entries in the journal of the corporation showing the method by which the transaction between Mr. E. J. Lord and the corporation was carried on?

A. They are.

Q. And they are photostatic copies of the journal of the corporation?

A. Yes.

Q. And they carry the journal entries from February 28, 1930, the date of the first payment to Mr. Lord, down through May 31, 1931?

A. That's right.

Mr. WRENN: I offer the group of photostatic copies of the journal account as one exhibit.

(Documents offered in evidence, consisting of nine pages, received and marked: "Taxpayer's Exhibit 32.")* [72]

Q. From the books of the corporation have you prepared a statement showing an analysis of the money that was distributed to Mr. E. J. Lord out of the capital and surplus of the company?

A. I did.

Mr. WRENN: I offer statement showing analysis of the moneys paid to Mr. E. J. Lord as an exhibit.

(Documents offered in evidence received and marked: "Taxpayer's Exhibit 33A" and "Taxpayer's Exhibit 33B," respectively.)

*Omitted from printed record on stipulation by counsel.

(Testimony of George Buchholtz.)

TAXPAYER'S EXHIBIT 33 A - B

STATEMENT SHOWING ANALYSIS OF \$468,219.98 Distributed to E. J. LORD BY E. J. LORD LTD. OUT OF CAPITAL AND SURPLUS.

Surplus Balance 12/31/29, plus 1930 profits (excluding 1930 Dividends)	676,032.63
Less Net Amount of 1930 profit not subject to 60% apportionment (As Exhibit -A-) attached	35,380.17
	<hr/> 640,652.46 <hr/>
60% of above \$640,652.46 due E. J. Lord	384,391.48
Plus Allowance for miscellaneous Equipment Charged to Contract Expense	3,500.00
Plus Allowance of 40% of Income Tax (as per Agrmt)	20,328.50
	<hr/>
Portion of SURPLUS distributed to E. J. Lord	408,219.98
60% " Capital " " "	60,000.00
	<hr/>
TOTAL DISTRIBUTION TO E. J. LORD (re 600 shares)	<hr/> 468,219.98 <hr/>

[Endorsed]: No. 2052. Filed February 1, 1932 at 11:40 o'clock A. M. (Sgd.) Robert Parker, Jr., Clerk, Supreme Court. [303]

(Testimony of George Buchholtz.)

EXHIBIT "A"

1930 Profits NOT subject to 60% Apportionment		
Profit from Contracts:		38,225.61
Hawaiian Pine Job	12,107.13	
Nawiliwili Wharf Road	12,243.28	
Kapaa Swamp	6,299.95	
Rodger's Airport	5,609.05	
Sundry Contracts	1,966.20	
		<hr/>
Plus Sundries, (Interest, Plant Rental etc.)		57,027.44
		<hr/>
		95,253.05
Less Discount on Bonds	1,525.00	
" Expense Accounts	52,254.02	53,779.02
		<hr/>
		41,474.03
Less Portion of Tax reserve (Not		
Applicable to E. J. Lord)		6,048.81
		<hr/>
		35,425.22
Less Difference on Contracts per Auditor's Re-		
port of 7/31/30 as compared with books		45.05
St. Louis Heights, Naw. Wharf & Kapalama		
Wharf		
Auditor's Report	153,331.90	
As per Books	153,286.85	
		<hr/>
		45.05
		<hr/>
NET PROFITS FOR 1930 PER BOOKS		
(not participated in by E. L. Lord)		35,380.17

[304]

Q. I will ask you to examine Taxpayer's Exhibit 33A and 33B and tell us how much was actually paid to Mr. E. J. Lord in the matter of the redemption of these 600 shares of stock?

A. \$468,219.98.

(Testimony of George Buchholtz.)

Q. How much of that sum represents what was paid from the capital account?

A. Sixty thousand dollars.

Q. And sixty thousand dollars represents the original capital contribution at the time of the incorporation of E. J. Lord, Limited?

A. That's right.

Q. And the difference between the \$60,000. and \$468,219.98 is income taken from the surplus account?

A. Yes.

Q. Upon which a Territorial income tax has been paid by the corporation?

A. Yes. [73]

Q. And the difference between the sixty thousand dollars and the \$468,219.98 is \$408,219.98 paid out of the surplus account, upon which a Territorial income tax of two per cent. has been paid?

A. That is right.

Q. Were all the payments made to E. J. Lord made in cash?

A. No.

Q. How were some of the payments to him made?

A. Part of them in bonds.

Q. And when he was paid in bonds you figured the book value of the bonds as of the date of the payment?

A. No, at par value, which was agreed upon.

Q. It was agreed upon in your original agreement?

(Testimony of George Buchholtz.)

A. Yes.

Q. Also considering the accrued interest, if any, on the bonds?

A. Yes.

Q. Have you prepared any statement other than the receipts, which show when bonds were paid to Mr. E. J. Lord or do the receipts fully show that?

A. The receipts fully show that.

Q. Please examine Taxpayer's Exhibit 15 and 16. Do taxpayers' Exhibits 15 and 16 show the methods by which payment was made and in what specie payment was made to Mr. E. J. Lord?

A. Yes. [74]

Q. But, whether paid in cash or by bonds, the entire payment to him of \$408,219.98 was out of surplus, representing profits, upon which a Territorial income tax of two per cent. had been paid?

A. Yes.

Q. In figuring the amount due Mr. E. J. Lord on the redemption of the stock I note you have considered the income of E. E. Black, Limited, for the 12 months preceding January 1, 1931. Just how was it that the share of Mr. E. J. Lord under the agreement was figured in the income of E. E. Black, Limited, for the 12 months of 1930.

A. Mr. Lord was interested in a certain amount of contracts; in fact, five of them that were not completed until sometime in 1930.

Q. Have you made an analysis of those contracts?

A. I have.

(Testimony of George Buchholtz.)

Q. Is that Exhibit A, which is attached to Taxpayer's Exhibit 33?

A. Yes.

Q. And were all the contracts in which Mr. Lord was interested completed during the year 1930?

A. Yes, sir.

Q. Subsequent to the year 1930 was there an adjustment under the provisions of the agreement of December 13, 1929 made with Mr. Lord for the payment of the [75] Federal income tax?

A. I didn't understand the first part of the question, quite.

(Question read by the reporter.)

A. Yes, sir.

Q. How much was paid him for that purpose?

A. \$20,328.50.

Q. What does the item of \$3,500. represent in Taxpayer's Exhibit 33?

A. That was an agreement that was reached in connection with that difference on the valuation of their plant, and it was finally compromised to pay Mr. Lord \$3500. extra.

Q. Does that \$3500 that you have there represent profits of the corporation upon which a Territorial income tax of 2 per cent. had been paid?

A. Yes.

Mr. WALSH: What does this income tax of 2 per cent. represent? It is down here 5 per cent.

Mr. WRENN: What return are you referring to?

(Testimony of George Buchholtz.)

Mr. WALSH: All of them.

The WITNESS: Five per cent. is right.

Mr. KAY: One provision was amended and the other was not. The rate was amended to five, and I assume you are referring to that exception set forth.

Mr. PETERS: Just using the words of the Statute, the Statute itself was never expressly amended. [76] As long as you pay 2 per cent., if you pay three more, you are exempt.

Q. However, for the purpose of the record, for the years 1926 to 1930, both inclusive, the corporation income tax that was paid was five per cent.?

A. I think it was right along.

Q. Whatever the rate was that was paid, the profit and loss which is reflected in your surplus account paid the Territorial corporation income tax during all those years?

A. Yes.

Q. I call your attention to Taxpayer's Exhibit 30 showing the ledger account of Treasurer's,—treasury stock purchase account. Will you explain why it was you carried this treasury stock purchase account down to the time the stock was finally paid?

A. There was no ascertaining what amount would be paid; first of all on account of the uncompleted contracts, and, second, it could not be ascertained until the books were closed and the taxes were figured out.

(Testimony of George Buchholtz.)

Q. Until the stock had been fully redeemed by the corporation from Mr. E. J. Lord, you carried this entire transaction in a stock purchase account?

A. Yes.

Q. And as soon as it had been fully redeemed you applied to the Treasurer for a reduction of the capital stock?

A. Yes. [77]

Q. And prior to petitioning the Treasurer of the Territory of Hawaii for a reduction of the capital stock of the corporation from one hundred thousand to forty thousand dollars you had been advised by Mr. MacComisky and Mr. Camp there was no Territorial income taxes due, and the amount distributed to Mr. Lord?

A. Yes.

Q. I have asked you to examine a statement entitled: "E. J. Lord, Limited, statement of surplus account from September 1, 1926, the date of incorporation, to date of December 31, 1930, showing reconciliation with Territorial income tax returned and amount of corporation income tax assessed on the profits of the company." E. J. Lord, Limited, is a misnomer, is it not. It is now known as E. E. Black, Limited?

A. Yes, sir.

Q. Was this statement prepared by you and Mr. H. W. Camp?

A. It was.

Q. Does it reflect the condition of the surplus account of the corporation from 1926 to the end of 1930?

(Testimony of George Buchholtz.)

A. Yes, sir.

Q. And the amount of the balance in the surplus account, amount credited to surplus account in each of the years 1926, 1928, 1929 and 1930?

A. Yes.

Q. Does this statement show the amount of net taxable [78] income as shown on the Territorial income tax return for the 12 months preceding January 1, 1927 for the calendar years 1927, 1928, 1929 and 1930?

A. Yes, sir.

Mr. WRENN: I offer this sheet in evidence.

(Document offered in evidence received and marked: "Taxpayer's Exhibit 34.")

TAXPAYER'S EXHIBIT 34

E. J. LORD, LIMITED

STATEMENT OF SURPLUS ACCOUNT FROM SEPTEMBER 1, 1926, THE DATE OF INCORPORATION, TO DECEMBER 31, 1930, SHOWING RECONCILEMENT WITH TERRITORIAL INCOME TAX RETURNS AND AMOUNT OF CORPORATION INCOME TAX ASSESSED ON THE PROFITS OF THE COMPANY.

Line No.	Surplus at Sept. 1, 1926 Date of In-corp'n.	1926	1927	1928	1929	1930	Grand Totals
1.	Gross Income per Tax Return	\$16,966.10	\$1,111,352.11	\$340,102.48	\$220,504.13	\$681,509.48	\$2,370,434.30
2.	Total deductions per tax return	11,453.53	1,041,729.15	12,989.03	132,047.43	76,373.20	1,274,592.34
3.	Net taxable income	5,512.57	69,622.96	327,113.45	88,456.70	605,136.28	1,095,841.96
4.	Plus Non-taxable items						
	Reserve for taxes debits			12,965.53	57,077.16	20,000.00	90,042.69
	Bad Debts			23.50			23.50
	Int. on Exempt Bonds				1,865.62	4,607.59	6,473.21
5.	Total	5,512.57	69,622.96	340,102.48	147,399.48	629,743.87	1,192,381.36
	Less non-deductible items						
	Donations		210.00	63.80	325.00	275.00	873.80
	Reserve for taxes-credits			57,000.00	20,077.16	101,616.74	178,693.90
	Bad Debt			23.50			23.50
	Accrued Int. on bonds				1,299.38		1,299.38
6.	Net Profit per books	5,512.57	69,412.96	283,015.18	125,597.94	527,852.13	1,011,490.78
7.	Surplus Account						
	Add Credits—Cr. Bl. 1st of Yr.	5,818.51	11,331.08	15,144.04	177,258.56	148,180.50	5,818.51
	Profit—Line 6	5,512.57	69,412.96	283,015.18	125,697.94	527,852.13	1,011,490.78
	Reserve for taxes			2,634.47			2,634.47
8.	Deduct Debits	11,331.08	80,744.04	300,793.69	302,956.50	676,032.63	1,019,943.76
	Dividends Paid						
	Good Will						
	Reserve for taxes		50,000.00	100,000.00	150,000.00	25,000.00	325,000.00
	Adjust. Ins. Policy		15,600.00	23,535.13			23,535.13
9.	Balance Surplus Account	11,331.08	15,144.04	177,258.56	4,776.00	651,032.63	15,600.00
10.	Territorial Income Tax Assessed vs. Corporation 5% on line 3	275.63	3,481.15	16,355.67	4,422.84	30,256.81	4,776.00
		275.63	3,481.15	16,355.67	4,422.84	30,256.81	54,792.10

[Endorsed]: No. 2052. Filed February 1, 1932

at 11:40 o'clock A. M. (Sgd.) Robert Parker, Jr.,

Clerk Supreme Court.

(Testimony of George Buchholtz.)

Q. I note that on March 12, 1931, there was filed with the Treasurer of the Territory of Hawaii an application to reduce the capital stock of E. E. Black, Limited, from \$100,000. to \$40,000. why was it that this application was not filed prior to this time?

A. It was done within less than a week's time after the books had been closed, and it had been ascertained the amount to be paid by Mr. Lord on account of taxes.

Q. In other words, you postponed this until the amount for the redemption of the stock had been paid?

A. It couldn't have been done before.

Q. I call your attention to the statement in regard to the redemption of the 600 shares of stock. You have examined that before?

A. Yes.

Q. It contains a resume of the journal entries of how this transaction was carried on to January 1, 1931? [79]

A. Yes.

Mr. WRENN: I offer this in evidence.

(Document offered in evidence received and marked: "Taxpayer's Exhibit 35A and "Taxpayer's Exhibit 35B.")

(Testimony of George Buchholtz.)

TAXPAYER'S EXHIBIT 35**E. J. LORD, LIMITED****JOURNAL ENTRIES RE REDEMPTION 600 SHARES STOCK**

Date	Journal	Dr.	Cr.
Feb. 28, 1930	Treasury Stock—Purchase a/c	\$273,855.36	
	To E. J. Lord—Settlement a/c		\$273,855.36
Jr.-5	To set up, as of 1-1-30, the initial amount to be paid to Mr. E. J. Lord for his shares in terms of the agreement dated 12-13-29—i.e., 60% of the net worth of E. J. Lord, Ltd. as of 12-31-29.		
Feb. 28, 1930	E. J. Lord—Settlement a/c	249,000.00	
	to Notes Receivable		100,000.00
	Bonds		119,000.00
	Investments		30,000.00
Jr.-5	To record the transfer of the above stated assets to Mr. E. J. Lord's a/c, as a partial settlement of the amount payable at the termination of the option in terms of the agreement dated 12-13-29.		
July 31, 1930	E. J. Lord—Settlement a/c	23,482.36	
	to Bonds		23,000.00
Jr.-69	Expense Interest		482.36
	To charge former a/c as per agreement.		
Dec. 31, 1930	Treasury Stock—Purchase a/c	175,313.98	
	To E. J. Lord Settlement a/c		175,313.98
Jr.-129	Final payment for 600 shares of E. J. Lord Co. stock.		
Dec. 31, 1930	E. J. Lord—Settlement a/c	108,277.86	
	To Investments		39,000.00
Jr.-129	Bonds		68,000.00
	Interest on Bonds		607.50
	Expense Interest		670.36
Dec. 31, 1930	Expense Interest	670.36	
	Interest on Bonds	607.50	
Jr.-139	to E. J. Lord Settlement a/c		1,277.86
	Supplementary to final settlement.		
Feb. 28, 1931	Treasury Stock	26,904.66	
	To E. J. Lord—Tax a/c		26,904.66

(Testimony of George Buchholtz.)

Jr.-17	Being 40% of Lord's Inc. Taxes in connection with redemption of his 600 shares (as per agreement) payable when due.		
Feb. 28, 1931	Surplus	476,074.00	
	to Treasury Stock		476,074.00
	To close latter a/c on a/c of redemption of stock.		
			[306]
May 31, 1931	Capital Stock	60,000.00	
	to Surplus		60,000.00
Jr.-41	Reduction of Capital Stock by redemption of 600 shares, approved by Treas., Territory of Hawaii, May 29th as of Mar. 12th, 1931.		
May 31, 1931	E. J. Lord—Settlement a/c	6,576.16	
	to Treasury Stock		6,576.16
Jr.-45	Difference original 40% of return \$26,904.66 and corrected \$20,328.50.		
May 31, 1931	Treasury Stock	6,576.16	
	to Surplus		6,576.16
Jr.-45	To transfer former a/c		6,576.16

[Endorsed]: No. 2052. Filed February 1, 1932 at 11:40 o'clock A. M. (Sgd.) Robert Parker, Jr., Clerk Supreme Court. [307]

Q. You brought with you the minute book of the corporation?

A. Yes, sir.

Mr. WRENN: I find that all of these minutes have not been copied by my stenographer. I will offer all the minutes at the next session.

(Adjourned to 8:30 o'clock a.m., Saturday, December 5, 1931.) [80]

[Title of Court and Cause.]

The above entitled matter came duly on for further hearing before the aforesaid Board on Saturday, December 5, 1931, at 8:30 o'clock a.m., before

(Testimony of George Buchholtz.)

the aforesaid Board, all members of the Board and all parties to the hearing being present, and the following further proceedings were had and testimony taken:

Mr. WRENN: I would like at this time to make a part of the record a letter that I asked for and obtained from Dr. Nils P. Larsen this morning relative to the physical condition of Mr. E. J. Lord. We are not going to have him testify because of his physical condition. We had him examined yesterday by Dr. Larsen and this letter fully explains his condition.

Mr. KAY: No objection.

Mr. WRENN: May this letter be made part of the record.

(Letter from Dr. Nils P. Larsen, dated December 4, 1931, offered in evidence, received and marked: "Taxpayer's Exhibit 36.")* [81]

Mr. WRENN: At this time I offer in evidence as one exhibit the minutes of the meetings of the shareholders of E. J. Lord, Limited, February 15, 1930, February 28, 1930, and March 7, 1931. We have these in lieu of the originals. We have the originals here.

(Documents offered in evidence received and marked, respectively, "Taxpayer's Exhibit 37A," "Taxpayer's Exhibit 37B," and "Taxpayer's Exhibit 37C.")

*Omitted from printed record on stipulation by counsel.

(Testimony of George Buchholtz.)

TAXPAYER'S EXHIBIT 37-A

SPECIAL MEETING OF STOCKHOLDERS OF
E. J. LORD, LIMITED.

Time: February 15th, 1930.

Place: The place of business of the company,
Pohukaina Street, Honolulu, T. H.

A special meeting of the stockholders of E. J. Lord, Limited was called to order by the President on February 15th, 1930 at 11 o'clock A. M. at the place of business of the Company, Pohukaina Street, Honolulu, T. H.

E. J. Lord, President, presiding.

The undersigned Secretary acting as secretary.

Upon roll call it was found that all of the members of the company were present personally and represented all of the outstanding shares of the stock of the company, to-wit, 400 shares, that is to say:

E. E. Black owning and representing 396 shares

E. J. Lord owning and representing 1 share

Geo. Buchholtz

owning and representing 1 share
(by proxy to Geo. Buchholtz

P. J. Erben (owning and representing 1 share

T. Ikejiri owning and representing 1 share

All of the members of the corporation there present thereupon signed the following written consent to said meeting:

We, the undersigned constituting all the members of E. J. Lord, Limited present at the meeting of which the within are minutes, consent to

(Testimony of George Buchholtz.)

this meeting and in token of said consent subscribe our names hereto.

(Sgd.) E. J. LORD

(Sgd.) E. E. BLACK

(Sgd.) GEO. BUCHHOLTZ

(Sgd.) P. J. ERBEN—by power of
attorney to Geo. Buchholtz

(Sgd.) T. IKEJIRI

No. 2052. Filed February 1, 1932 at 11:40 o'clock
A. M.

ROBERT PARKER, JR.,

Clerk Supreme Court. [308]

The following resolution was duly offered and
unanimously carried:

“RESOLVED by the stockholders of E. J. Lord, Limited that the Articles of Association of the corporation be amended so that the name of the corporation appear therein as ‘E. E. Black, Limited’ instead of ‘E. J. Lord, Limited,’ and that the title and Articles 1 and 8 respectively read as follows:

‘ARTICLES OF ASSOCIATION

—of—

E. E. BLACK, LIMITED’

‘1. The name of the company is and shall be
‘E. E. BLACK, LIMITED.’

‘8. The Company shall have succession and corporate existence for the term of fifty (50) years from the date of these presents and become a body corporate under the name and

(Testimony of George Buchholtz.)

style of 'E. E. Black, Limited,' and subject to all the liabilities provided by law for incorporated companies, and shall be subject to and have all the benefits of all general laws now and hereafter enacted in regard to corporations. All the property of the Company shall be liable for the just debts of the Company, but no shareholder shall be liable for the debts of the Company beyond the amount of what is due upon the share or shares owned by him.'

RESOLVED, FURTHER, that the proper officers of this company be, and they are hereby authorized and directed to make application to the Treasurer of the Territory of Hawaii in accordance with law for the allowance and confirmation of the amendments aforesaid and to make and file all such affidavits and other instruments as may be necessary or proper to effectuate the purpose, intent and direction of this resolution."

There being no further business, upon motion duly made and carried, the meeting adjourned.

(Sgd.) T. IKEJIRI,

Secretary. [309]

(Testimony of George Buchholtz.)

TAXPAYER'S EXHIBIT 37B

MINUTES of the annual Meeting of Shareholders of E. E. Black, Ltd., held at the office of the Company in Honolulu on February 28th, 1930 at 3 P. M.

PRESENT:

Mr. E. E. Black	(owning 400 shares)
“ Geo. Buchholtz	(by invitation)
“ T. Ikejiri	(“ “)

All outstanding Shares being represented, the meeting came to order.

MINUTES of February 15th, 1930.

The Minutes of the Special Meeting of February 15th, 1930 were read, and approved as read.

AMENDMENT OF ARTICLES OF ASSOCIATION:

E. E. Black stated that the amendment to the Articles of Association had been amended to change the name of the Company to E. E. Black, Limited, and had been granted and approved by the Governor of the Territory of Hawaii, and directed that a copy of the Amendment be affixed in the Minute book.

ELECTION OF DIRECTORS AND AUDITORS:

and Messrs. Young, Lambertson & Pearson as auditors.

There being no further business the meeting adjourned.

(Sgd.) T. IKEJIRI. [310]

MINUTES of the annual Meeting of Stockholders' of E. E. Black, Ltd., held at the office of the Company on March 7th, 1931 at 9:30 A. M.

E. E. Black, Ltd.) “ 600 “

The Minutes of the Meeting of Stockholders of February 28, 1930 were read, and approved as read.

(Testimony of George Buchholtz.)

AUDITOR'S REPORT:

The Auditor's report dated March 3rd, 1931 was submitted and read, including Auditor's Certificate and Balance Sheet as of December 31, 1930.

Mr. Black moved that the Auditor's Report be approved and filed in the Minute Book as part of the Minutes.

ELECTION OF OFFICERS:

Mr. Buchholtz nominated the following directors, there being no further nomination, the Secretary was asked to cast the ballot.

Mr. E. E. Black

Mr. P. J. Erben

Mr. Geo. Buchholtz

Mr. T. Ikejiri

Mr. R. J. Davis

carried unanimously.

ELECTION OF AUDITOR:

Mr. Black moved that Messrs. Young, Lambertson & Pearson be re-elected.

Mr. Buchholtz seconded the motion, carried unanimously.

REDUCTION OF CAPITAL STOCK:

Mr. Black moved that the following resolution be passed:

"WHEREAS E. E. Black, Ltd. has an authorized Capital [311] Stock of \$100,000. divided into 1,000 shares of the par value of \$100. each and has purchased from one of its

(Testimony of George Buchholtz.)

stockholders 600 of said shares of the par value of \$100. each, of the aggregate par value of \$60,000.—, and has paid for the same and holds the same in its treasury and desires to retire said 600 shares and reduce its capital stock accordingly to \$40,000.—divided into 400 shares of the par value of 100 each,

THEREFORE BE IT RESOLVED that the authorized capital stock of E. E. Black, Ltd., be reduced from \$100,000.—divided into 1,000 shares of the par value of \$100.—each to \$40,000.—divided into 400 shares of the par value of \$100.—each by retiring 600 shares of the par value of \$100.—each now held in the treasury;

That a sworn certificate signed by the presiding officer and secretary of this meeting be presented to the Treasurer of the Territory of Hawaii setting forth therein the action taken and certifying that at the time the vote on this resolution was taken the corporation was not and has not since become indebted in any manner over and above half of the amount of its remaining capital stock;

AND BE IT FURTHER RESOLVED that when the said reduction of capital stock is effected as required by law, the Treasurer of this corporation do retire and cancel the said 600 shares of the par value of \$100. each of this corporation now held in the Treasury.”

(Testimony of George Buchholtz.)

Mr. Buchholtz seconded the motion, carried unanimously.

There being no further business, the meeting adjourned.

[Seal]

(Sgd.) T. IKEJIRI,

Secretary. [312]

Mr. WRENN: I offer in evidence at this time as one exhibit minutes of the Board of Directors of E. J. Lord, Limited, dated December 7, 1929, February 28, 1930 and December 20, 1930.

(Documents offered in evidence received and marked, respectively, "Taxpayer's Exhibit 38A," "Taxpayer's Exhibit 38B," and "Taxpayer's Exhibit 38C.")

TAXPAYER'S EXHIBIT 38-A

MINUTES of a Special Meeting of the Board of Directors of E. J. Lord, Ltd., held at the office of the Company in Honolulu, T. H., on December 7th, 1929 at 10 A. M.

PRESENT:

Mr. E. E. Black

Mr. Geo. Buchholtz

Mr. T. Ikejiri

CHAIRMAN:

Mr. E. E. Black, Vice-President of the Company, took the Chair and called the meeting to order.

(Testimony of George Buchholtz.)

MINUTES OF MAY 31st:

The minutes of the meeting of May 31st were read, approved, and ordered placed on file.

PURCHASE OF STOCK:

Mr. E. E. Black moved that as Mr. E. J. Lord was willing to sell all his stock of E. J. Lord, Ltd. the Company was to redeem the 600 shares for which the Company was to pay for the said shares in the following manner:

(1) The sum of money equal to 60% of the net worth of the Company as of December 31st, 1929.

(2) The sum of money equal to 60% of the net profits of all contracts awarded and not completed on December 31, 1929.

(3) The sum of money equal to 40% of the amount to which Mr. E. J. Lord may become liable for Federal and Territorial Income Taxes upon income accrued and to accrue to him resulting from the sale of said 600 shares.

Mr. Lord agreed to give the Company an option to purchase the above mentioned stock to February 28th, 1930, and to have an agreement drawn signed by both parties covering the above option, price and payments to be made, a copy of such agreement to be entered into the Minute-book. Mr. Geo. Buchholtz seconded the motion which was carried unanimously.

Mr. Buchholtz moved that the Company upon the exercise of the option cause its articles of

(Testimony of George Buchholtz.)

Association to be amended so that the name does not contain the name "E. J. Lord" or any words similar to said name. [314]

Mr. Black seconded the motion to be carried unanimously.

ADJOURNMENT:

There being no further business, the meeting adjourned.

(Sgd.) T. IKEJIRI,
Secretary.

[Endorsed]: No. 2052. Filed February 1, 1932 at 11:40 o'clock A. M. Robert Parker, Jr., Clerk, Supreme Court. [315]

TAXPAYER'S EXHIBIT 38-B

Meeting of Directors of E. E. Black, Ltd., held in Honolulu, February 28th, 1930 at 3:15 p.m.

PRESENT:

Mr. E. E. Black
" Geo. Buchholtz
" T. Ikejiri
" R. J. Davis
" Frank Jose

CHAIRMAN:

Mr. Black took the chair and called the meeting to order. The Chairman stated that a majority of the Directors were present and met by consent.

(Testimony of George Buchholtz.)

ELECTION OF OFFICERS:

Mr. Black moved that the following officers be elected, seconded by Mr. Buchholtz and carried unanimously.

Mr. E. E. Black, President

“ P. J. Erben, Vice-President

“ Geo. Buchholtz, Treasurer

“ T. Ikejiri, Secretary

AUDITORS REPORT:

The Auditors Report dated January 29th, 1930, with Balance Sheet as of 12-31-1929 was submitted and read. Mr. Ikejiri made the motion, and seconded by Mr. Black that the Auditor's Report be approved and placed on file in the minute book.

TREASURY STOCK:

Mr. Buchholtz stated that Mr. E. J. Lord had turned in his 600 shares on February 15th, 1930, and had been paid \$250,000.00 on account, with interest from January 1st, 1930 to February 15th, 1930, as per agreement.

ADJOURNMENT:

There being no further business the meeting adjourned.

(Sgd.) T. IKEJIRI,
Secretary. [316]

(Testimony of George Buchholtz.)

TAXPAYER'S EXHIBIT 38-C

MINUTES of a Special Meeting of the Board of Directors of E. E. Black, Ltd. held at its office on December 20th, 1930 at 10 A. M.

PRESENT:

Mr. E. E. Black, President
“ Geo. Buchholtz, Treasurer
“ T. Ikejiri, Secretary

CHAIRMAN:

Mr. Black took the chair, there being a quorum present, called the meeting to order.

MINUTES of December 5th, 1930:

The minutes of the special meeting of December 5th, 1930 were read, approved and ordered placed on file.

MR. FRANK JOSE REMOVED AS DIRECTOR:

Mr. Ikejiro moved that whereas Mr. Frank Jose was no longer in the employ of the Company, he be removed as a Director, Mr. Black seconded the motion, carried unanimously.

FINAL SETTLEMENT WITH MR. E. J. LORD:

Mr. Buchholtz read the Auditor's Report to July 31st, 1930 as well as Mr. MacComiskey's letter re. Taxes, dated December 17th, 1930, as well as a yet unmailed letter to Mr. Lord of December 19th, 1930, showing that Mr. Lord's share in the final settlement from the above reports came to \$170,536.12 with additional

(Testimony of George Buchholtz.)

\$3,500.00 for Plant, as agreed in meeting of December 5th, 1930, making a total of \$174,-036.12.

Mr. Ikejiri moved that the above mentioned letter be mailed to Mr. Lord, and that copies of the mentioned reports and letters be placed in the Minute book, and that the treasurer be directed to pay to Mr. Lord the sum of \$174,-036.12 in Bonds and Cash, as set forth in letter to Mr. Lord, dated December 19th, 1930, and receive from Mr. Lord therefor a receipt in full settlement, with the proviso, that the 40% of Federal and Territorial Income Taxes, to which Mr. Lord becomes liable upon income accrued by reason resulting from the sale of the 600 shares of E. J. Lord, Ltd., will be paid upon assessment, as per agreement of December 13th, 1929.

BONUS TO MR. BLACK:

The Treasurer stated that the financial condition of the Company, after having settled with Mr. E. J. Lord, was very sound, and stated that the Profits on the Completed Contracts to November 30th, 1930 were \$620,612.35, less proportion of Operating Expenses of \$35,081.10, leaving a Net Profit on the above mentioned Contracts of \$585,531.25.

Mr. Buchholtz moved that Mr. Black be paid a Bonus of two per cent on the above mentioned Net Profit of \$585,531.25, making a sum of

(Testimony of George Buchholtz.)

\$11,710.60. Mr. Ikejiri seconded the motion, carried unanimously. Mr. Black directed the treasurer to pay the above amount.

ADJOURNMENT:

There being no further business, the meeting adjourned.

(Sgd.) T. IKEJIRI,
Secretary. [317]

Mr. WRENN: With the consent of the attorneys for the Government we would like to have the appeal amended by inserting the words "E. J. Lord" after the word "Taxpayer" on the last line of page 2 of the appeal.

Mr. PETERS: Do you consent that the word be written in by the Board?

Mr. KAY: Yes. I have no objection.

H. W. CAMP

was duly called and sworn as a witness for the Taxpayer, and testified as follows: [82]

Direct Examination by Heaton L. Wrenn, Esq.

Q. Will you state your name, please.

A. H. W. Camp.

Q. You are assistant secretary of Hawaiian Trust Company, Limited?

A. I am.

(Testimony of H. W. Camp.)

Q. And is Hawaiian Trust Company, Limited, the agent for Mr. E. J. Lord?

A. It is.

Q. And as agent for Mr. E. J. Lord did you prepare his tax return for the 12 months preceding January 1, 1930?

A. I did.

Q. And that return was filed within the time prescribed by law?

A. It was.

Q. I call your attention to the original returns. Prior to making this return did you examine the surplus account of the corporation which is now known as E. E. Black, Limited?

A. Yes.

Q. And with reference to the surplus account did you also examine the profit and loss account of that corporation?

A. I did.

Q. What was the cost of Mr. Lord's stock in the corporation,—sixty thousand dollars?

A. That was the cost that I returned. [83]

Q. And you show that in the return, do you?

A. Yes.

Q. You have examined the assessment that was made by the tax assessor in this matter?

A. I have.

Q. And the assessment that was made by the tax assessor after the filing of the original return and after the filing of the amended return also allows

(Testimony of H. W. Camp.)

this sixty thousand dollars as the cost of the stock?

A. It does.

Q. Did you make a computation to determine how much was received by Mr. Lord from the corporation pursuant to the agreement of December 13, 1929, over and above his original capital contribution of sixty thousand dollars?

A. Yes.

Q. Is that computation a computation that was made by you,—is that attached to the return?

A. Yes, that has been furnished to the tax office.

Q. You likewise made a supplemental return, did you not?

A. I did.

Q. In making this computation did you prepare an analysis, working in conjunction with Mr. Buchholtz, of the surplus account of the corporation?

A. Yes.

Q. The difference between the total amount of \$468,000., in round figures, so received from the [84] corporation by Mr. Lord, and the sixty thousand dollars representing his original contribution, came entirely from the surplus account, did it not?

A. It did.

Q. Can you say from your analysis of the surplus account as to whether this is from the profits of the corporation, this difference?

A. Yes, the profits were transferred out of the profit and loss account to the surplus account.

(Testimony of H. W. Camp.)

Q. So the figure of \$406,569.98 which you have set forth in your supplemental return and schedule attached thereto represent profits of the corporation which were taken out of the surplus account and distributed to Mr. Lord?

A. That is correct, and the total account distributed there was \$1,650. in excess of \$406,569.98, that being due to certain attorney's fees which were considered as an expense to Mr. Lord on his tax return.

Q. And that expense was allowed by the assessor in making his assessment, was it not?

A. It was.

Q. And the \$406,000. plus the \$1650. making \$408,000. in round figures, came entirely from the surplus account and was paid out of profits?

A. It did.

Q. In connection with your analysis of the surplus account you examined the tax returns of E. J. Lord, [85] Limited, for the 12 months preceding January 1, 1927, and for the taxation years 1927, 1928 and 1929, as well as the return for the 12 months preceding January 1, 1931, of E. E. Black, Limited?

A. Yes, sir.

Q. And from your examination of these returns and from your analysis of the reports could you testify whether or no the corporation paid a corporation Territorial income tax upon this income which was distributed to Mr. Lord out of the surplus account?

(Testimony of H. W. Camp.)

A. Yes, that is correct.

Q. A Territorial income tax was paid on that?

A. It was.

Q. Yesterday Mr. Buchholtz, when he was testifying, identified an analysis of the surplus account of the corporation, which is Taxpayer's Exhibit 34, and stated that this was prepared by you in conjunction with him,—that is correct?

A. Yes, that is correct.

Q. What does Taxpayer's Exhibit 34 purport to show?

A. That exhibit was prepared in order to show that the corporation has paid an income tax on all of the profits with the exception, of course, of minor non-taxable and non-deductible items of the surplus.

Mr. PETERS: Non-taxable and deductible.

A. Non-taxable and non-deductible items,—showing that the company has paid an income tax on all of [86] that surplus with those exceptions, which has been paid over to Mr. Lord in settlement for the retired stock.

Q. In making this return you had access to the books of the corporation for the years involved?

A. Yes, and the office copies.

Q. And it is a photostatic copy of this that is now in evidence?

A. That is correct.

Mr. ADAMS: When you say "non deductible" you mean non-deductible from what?

(Testimony of H. W. Camp.)

A. Non-deductible from gross income.

Mr. ADAMS: If non-deductible it would be taxable, would it not?

A. Well, this schedule starts out with the gross income, as shown by the tax returns, and is adjusted from the non-taxable items and the non-deductible items under the Territorial law, resolving down to an agreement with the surplus account in the corporation accounts.

Mr. ADAMS: The non-deductible amounts being the amounts on which taxes are imposed?

A. That's correct.

Q. The dividend that was paid to Mr. Lord for his stock came out of this surplus account that you analyzed?

A. Yes, that's correct.

(Recess) [87]

Q. How long have you been connected with the Hawaiian Trust Company, Limited?

A. About 11 years.

Q. And during those entire eleven years what has been the nature of your work with the Hawaiian Trust Company?

A. My duties have been accounting and tax work,—tax accounting and also straight accounting.

Q. You are head of the tax department, are you not?

A. I am.

Q. And prior to going with the Hawaiian Trust Company in the year 1920 what experience, if any, did you have as an accountant?

(Testimony of H. W. Camp.)

A. I was connected with the firm then known as the Audit Company of Hawaii, now known as Young, Lambertson & Pearson, quite a number of years; about seven or eight years.

Q. What were your duties when you were connected with the Audit Company of Hawaii?

A. Duties of an auditor, senior auditor.

Q. In the event that E. H. Lord had declared a dividend, out of what account would it have declared this dividend?

A. It could only declare it out of surplus account, because all the profits of the company are transferred, under their bookkeeping system, to that account.

Q. And a dividend, if it had been declared, would have been charged against the surplus account?

A. It would have had to be so charged. [88]

Q. In the event that the corporation had declared a dividend of all its undivided profits in the surplus account what would have been the amount of that dividend at the end of 1929?

A. At the end of 1929 the surplus account showed a balance of \$148,180.50. If they had declared a dividend of the entire surplus account that would have been the amount.

Q. In addition to dividends charged against that account in the years 1927, 1928 and 1929—

A. There was no dividend in 1926. In 1927, 1928 and 1929 the dividends were charged to that ac-

(Testimony of H. W. Camp.)

count. I don't quite understand that last question. Will you state that again.

Q. This one hundred and five thousand dollars balance, in round figures, that you have testified to, would have been paid out of the surplus account in addition to the dividends which had already been declared in the previous years?

A. Yes, that is correct. There was a balance of \$148,000. roughly after paying of the dividends. Mr. Wrenn spoke of \$105,000. That amount, I believe, was \$148,000., the balance of surplus at the end of 1929.

Q. Of the \$468,000., in round figures, that was paid to Mr. E. J. Lord, sixty thousand dollars of that was declared out of the capital, was it not?

A. That is correct. [89]

Q. And the balance paid to him as a dividend of \$408,000. came out of surplus?

A. Yes.

Mr. ADAMS. May I ask a question? That surplus account of \$400,000. was earned profits?

A. Yes, the books of the company so reflect all of these items, with the exception of a small balance at the beginning of the surplus account, \$5,818.51. I didn't go into that figure. It may be earned profits, but all of the rest of the balance of that account is earned profits according to my analysis of the company's books.

Q. You have just stated that the balance in the surplus account at the close of 1929 was \$148,180.50.

(Testimony of H. W. Camp.)

Where did the balance of the \$408,000., in round figures, come from that was paid to him?

A. That balance was made up of additional profits on certain contracts completed in 1930, which were still pending and not taken into the surplus account at the end of 1929.

Q. And those profits from the uncompleted contracts were shown in the surplus accounts for the year 1930?

A. They were.

Cross Examination by Harold T. Kay, Esq.

Q. How long have you been acting as financial agent or otherwise for Mr. Lord?

A. I think our first duties in connection with Mr. [90] Lord's account started sometime in 1929, —at the close of 1929.

Q. At that time was Mr. Lord contemplating severing his connection with E. J. Lord, Limited?

A. That is something I cannot state. I don't know.

Q. Did he confer with you concerning the sale of his stock of E. J. Lord, Limited?

A. No, I didn't handle Mr. Lord's personal affairs in our office; merely his tax affairs. Those affairs are handled by other officers of the Trust Company.

Q. You made out the tax returns for Mr. Lord in 1929?

A. Not in 1929.

Q. 1930?

(Testimony of H. W. Camp.)

A. In 1931, based upon 1930 income.

Q. When did you have occasion to examine the books of E. J. Lord, Limited?

A. In connection with the preparation of Mr. Lord's returns in 1931.

Q. You made a complete examination of all the E. J. Lord, Limited books, did you?

A. Only of the surplus account.

Q. You had no occasion to examine the complete records of that company?

A. No, I made no complete audit. The books are audited by Young, Lamberton & Pearson. There was no necessity of my doing that.

Q. Do the books reflect the consideration that E. J. [91] Lord paid to E. J. Lord, Limited, for his 800 shares of stock issued to him in 1926?

A. My understanding is they do. I haven't examined the entries. I asked Mr. Buchholtz to inform me as to what had been paid in order to estimate the cost basis, and he gave me that information.

Q. What did the books show as the consideration paid by E. J. Lord for these 600 shares of stock sold by E. J. Lord?

A. They reflect the amount of \$468,000.

Q. That was the total consideration paid, was it?

A. I think so. That is shown in the settlement account which has already been filed as an exhibit and copy given to you.

(Testimony of H. W. Camp.)

Q. Do the books reflect a sale of that stock to the corporation for which the corporation pays the \$468,000?

A. The books do not mention a sale, as I recall it. They show that the stock was acquired from Mr. Lord and placed in their treasury account and subsequently that stock was redeemed.

Q. The books reflect that the corporation paid this \$468,000., do they not?

A. Yes, that was paid in cash and other assets.

Q. That was paid for the surrender of this 600 shares of stock by Mr. Lord?

A. That is correct, yes.

Q. What was the total amount of dividends paid by [92] E. J. Lord, Limited, as reflected by its books, in the year 1929?

A. \$150,000.

Q. In the year 1930?

A. \$25,000.

Q. In the year 1929 the books reflect a salary paid to E. J. Lord also, do they not?

A. I don't know.

Q. So that in the year 1930 the books reflect no dividends paid the stockholders other than the dividends of \$25,000?

A. I would not say that. There was a regular dividend paid out of the earnings of the company subsequent to the distribution from the surplus account to Mr. Lord in settlement for his stock. Mr. Lord did not participate, as I understand it, in the

(Testimony of H. W. Camp.)

ordinary dividends of \$25,000., those having been paid out of the profits after he received his distribution of the profits.

Q. Was there any distribution of capital or surplus, whichever name the cash resources of the company went under, to any of the other stockholders besides Mr. Lord?

A. No.

Q. Have you examined the minutes of the corporation?

A. To some extent.

Q. They reflect, do they not, that this amount of \$468,000. was paid to Mr. Lord in consideration of [93] his selling to the corporation his 600 shares of stock?

A. The minutes I saw refer to the settlement, the consideration that was paid to Mr. Lord as being a redemption of his stock.

Q. What was the reason for that redemption as reflected by the books?

A. You mean the account books or the minute books?

Q. Any records?

A. The accounting books do not show any reason for the corporation's redeeming Mr. Lord's shares and I do not recall seeing any definite reason in the minutes, excepting that the corporation wished to redeem these shares.

Q. You testified here you have been engaged in tax work for a long time and that you are now tax expert with the Hawaiian Trust Company?

(Testimony of H. W. Camp.)

A. Yes.

Q. The Territorial income tax imposes a tax on capital gains, does it not?

A. It does on the sale of assets.

Q. Assuming this situation, Mr. Camp,—Assume a stockholder owns 100 shares in Ewa Plantation and I sell or I buy those shares at \$35.; subsequently I sell those shares at \$40.,—the difference between the purchase price and the selling price constitutes a net capital gain to me, and on which I have to pay a Territorial income tax, does it not?

[94]

A. Yes.

Q. Now in Section 1391 the exemption stated by the Statute is directed to dividends paid on stock owned, is it not?

A. Section 1308, I believe, covers exemption of dividends.

Q. Referring you to Section 1391, the last proviso thereof, will you state whether or not that proviso provides “That in assessing the income of any person or corporation there shall not be included the amounts received from any corporation as dividends upon the stock of such corporation if the tax of two per centum has been assessed upon the net profits of such corporation”?

A. That provision so states, yes.

Q. This distribution to Mr. Lord was not in the nature of a duly declared dividend distributable to all the shareholders from net profits, was it?

(Testimony of H. W. Camp.)

A. It was not the same as a regular dividend paid out of earnings, paid to all stockholders, but I consider it was a dividend paid out of the profits of the company.

Q. You considered it a dividend and not a gain on capital?

A. Yes, that is what I judged it to be.

Q. You have stated you make out the income tax returns for E. J. Lord, have you not?

A. Yes. [95]

Q. Will you state whether or not the document I hand you is a true copy of the Federal income tax return made out by you for E. J. Lord for the year 1930?

Mr. WRENN. I object to any examination on the Federal income tax return because the Federal income tax laws provide that upon liquidation any gains that may be received by the taxpayer is taxable as a capital gain. It cannot have any bearing on this controversy existing under our Territorial income tax laws.

Mr. KAY. May it please the Board, I will show the relevancy of this examination as we proceed.

Mr. ADAMS: Would you mind telling us what relevancy this has, in your opinion?

Mr. KAY: I think it will develop, may it please the Court. It has a clear relevancy or I would not be offering it,—clearly material, and I can see no legitimate grounds for an objection to it.

Mr. WRENN: I think the legitimate ground for objection to it is that we are not concerned with

(Testimony of H. W. Camp.)

the Federal income tax laws, and this is a return for the Federal income tax law which is mandatory and upon which a tax has been paid. If it has any relevancy, I think we are entitled to know it at this time.

Mr. ADAMS: I think so too. What is the relevancy?

Mr. KAY: The relevancy is simply this: The contention [96] of this witness is that this distribution was a dividend and it was not a capital net gain. In the Federal income tax return made out by this witness for the taxpayer under Schedule "D" capital net gain from sale or loss from sale of assets, you have more than two years. There is listed 600 shares E. J. Lord, Limited, 1926 to 1930, that is the date acquired and date sold, \$599,743.20 as the amount realized from the sale of his capital assets. The cost and value as of March, 1931, sixty thousand dollars; subsequent improvements and capital deductions, \$1,650.; net gain or loss, 12½ per cent., \$538,093.20. Upon cross examination we certainly have the right to acquire into the evidence already adduced in respect to this witness, the authenticity of that evidence; whether or not the position assumed by the taxpayer in this case is consistent with the position assumed in respect to other matters, and also whether the amount of gain is the same in both cases. Counsel says that the Federal law is different from our law. Under the Federal law, may it please the Court, when stock

(Testimony of H. W. Camp.)

is sold to a corporation, being the corporation's own stock, a tax is imposed and it is recognized that under the income tax, properly speaking, a tax is assessable. That tax may be either upon the net gain as a liquidating dividend or upon the net gain from the sale of capital assets. If it is plain [97] there is a sale of capital assets, which is binding of course upon the Taxpayer when so claimed, the rate is only $12\frac{1}{2}$ per cent. Where there is a liquidating dividend, as that is called, upon dissolution or otherwise, there is a surtax, and where the amount runs into large figures the sur-tax may be considerably in excess of the $12\frac{1}{2}$ per cent. Now the taxpayer in this case has considered this sale of his stock as a sale of capital assets and he has made that representation to the Federal government, and it will be noted that the amount he enters up as a sale of capital assets is greater than in the case at bar. Now, under our law, as Mr. Camp has stated, a tax is imposable and assessable upon profits derived from the sale of capital assets, and in this case our contention is that this clearly is out and out a sale of capital assets; that the two parties in this controversy, to-wit, E. J. Lord, Limited and E. J. Lord, are two distinct entities. The law so recognizes them. You can tax the stock, you can tax the corporation. The stockholder has no tenable interest in the property of the corporation. He simply owns that stock, which represents an interest which may mature upon dissolution. But here we have a con-

(Testimony of H. W. Camp.)

tinuing corporation; the stockholder sells his stock to the corporation for a consideration; he makes a profit, [98] the difference between the amount paid by the corporation and the amount that he paid the corporation for the stock. So we say that under any view of the case the contention of the taxpayer here, to-wit, that this is simply a dividend that has already born its tax, is without bottom and has no merit in it, and, in corroboration of that, along with other facts which we intend to prove, we bring the Federal income tax return and we show there the position adopted by the taxpayer in respect to this particular transaction. That position has been a sale of capital assets and so considered by him.

Mr. WRENN: I do not think this Board wants to open up the field of Federal income tax law. If you wish to go into that field, we are perfectly willing to do that, but it is incompetent, irrelevant and immaterial. Mr. Kay says that the liquidating dividend under the Federal law is not taxed as a capital gain. The Federal tax law says liquidating income shall be taxed as a gain. We are not going to get any place in the ultimate issue here by delving into the Federal income tax laws and Federal income tax return, and that is why I object to going off on this tangent.

Mr. PETERS: May I say a word. I think from the standpoint of the Territory the question directed to the Board is whether or not the evidence of this witness [99] should be considered at its face value

(Testimony of H. W. Camp.)

by reason of the fact that he has treated the same subject matter in a different way on another occasion, which if properly done is in direct conflict with what he contends here. I just want to say this, that as far as this particular question is concerned, if the Federal tax law requires expressly that certain income on certain transactions be treated in a certain way, you must treat them in that way. That is all there is about it. For instance, the United States has provided relative to the question of capital gains, the valuation as it existed on the 1st of March, 1913, and on that basis the United States returns are computed. Our local statute provides another method of computing income. Now, the situation is that as far as the Federal law is concerned it has suffered four amendments in regard to treating these liquidating dividends, and in 1926 it amended the law so that it definitely required, it became mandatory that as far as these liquidating dividends are concerned they should be returned in a certain way. Now, if the question that Mr. Kay now propounds is directed to the attention of the Board for a showing that under identically similar circumstances and an identically similar law this witness made an entirely different analysis of the situation and returned it differently, that is one thing. [100] Then we have the prior contradictory statement made under identical similar circumstances. But that is not the situation here. Counsel cites a Federal statute. Before this Board can come to the con-

(Testimony of H. W. Camp.)

clusion that this witness has made a prior contradictory statement in regard to the same matter, it must find the major premises, that all the facts and circumstances are the same; otherwise it is not a contradictory statement. If we get into this 1926 amendment, then we must go back to the entire history of the law. This Board will be called upon, not alone to determine the legal phases of our Territorial law, but it will be called upon to determine the legal phases of our Federal law, and determine whether or not the Federal law is the same as our Territorial law, otherwise it would not be a contradictory statement and different treatment of the same subject matter. Mr. Kay's contention would not only bring the Board into a consideration of the very issue involved in this appeal, but, as an ancillary matter, it would call upon the Board to decide what the Federal law means, too. So you have not only the problem to determine what the local law means, but you have to determine what the Federal law means, and see if the Federal law contains a provision to meet this identical provision. We haven't anything in the local law relative to liquidating dividends. [101] We are applying section 1391 in the spirit of the law. That, as far as the individual is concerned, after he receives a dividend, he shall not again pay a tax on that dividend where the corporation has already paid it. When anything comes to the stockholder as his dividend, you cannot call it any other name. Whether it has

(Testimony of H. W. Camp.)

the direct authorization of the two people that own the corporation, to-wit, Lord and Black, it is a dividend, if the Board please, by whatever name you call it. To ask this witness why under these circumstances he made this particular return as to the Federal law in one way, and then returned it in respect to the Territorial law in another way, unless the laws are the same, unless the provisions are the same, we cannot consider it. We all know the arbitrary rules that have been fastened on us by the Federal law in regard to our income. In many instances there is neither rhyme nor reason in it, but we have to do it because they require it in a particular way. If we go into this entire proposition as counsel would like to have us go into it, we not alone have to go into the 1926 amendment, but we have to go into the 1917 amendment and the 1921 amendment and the relation that the three amendments, 1923, 1917 and 1926 bear to the original act of 1913, and every phase of the treatment of liquidating dividends by the United States will [102] have to be examined. I don't object, and, as far as we are concerned, we will welcome the opportunity to examine the Federal law and see how the Federal law has treated this particular subject,—not alone under the 1926 law, where the exact transaction has been taken up and disposed of by reason of the fact that the earlier amendments contained no reference to it. We welcome that. We welcome all the information the Board can get on this sub-

(Testimony of H. W. Camp.)

ject as to the Federal law or any other tax law. I do not care to have the record show here, or have the record encumbered with the attempt to show that Mr. Camp, after a study of the facts and circumstances of this particular case, has acted in respect to the same law differently.

Mr. ADAMS: Your contention is that what goes under the Territorial laws as liquidating dividend under the Federal law of 1926 must be classed as a capital account and therefore goes back to the value of that capital in 1913?

Mr. PETERS: Yes, so it has no application to the Territorial law whatever.

Mr. KAY: It seems as if we are getting the cart before the horse in this matter. My question was directed as to whether or not this return was a true copy. Lets find out wherein the Federal law differs from our law. Let's find out whether this return is based upon an entirely different law and [103] that facts stated in respect to that law are not applicable to our own law. The question of capital is a fact, not a question of law. It is a fact, and where representation is made of a certain transaction which results in a capital account, that is a fact. Our law taxes capital accounts. The Federal law, as you gentlemen are well aware, is apparently an out and out income tax law. Our law was modeled on the Federal law. The Legislature has from time to time directed that our administration officials follow as nearly as possible Federal adminis-

(Testimony of H. W. Camp.)

tration. In the case at bar there were two tax returns made,—one the Federal and the other the Territorial. In the contract between Mr. Black and E. J. Lord provision was made for apportionment of Territorial and Federal taxes. Now, in this apportionment evidently considerable consideration was given to the amount of taxes to be paid. True, our law is not the Federal law, and income and accounts taxable under our law must be considered only in the light of our law, regardless of what the Federal law may provide, or regardless of what the Federal administration might be. This Board is confined to the Territorial law, but our Territorial law provides for a tax upon capital accounts. Now it is within the province of the Territorial officials to exhaust every effort to ascertain whether or not there has [104] been a capital account in this case, and I submit that this Board would be abusing its discretion if it kept out of the record evidence of the character that we propose to introduce along this particular line.

Mr. PETERS: I might say in regard to that,—might I suggest a way out of the dilemma, to relieve the Board of any embarrassment at this time. I am directing my objection to any imputation, as far as this witness is concerned, that he has treated this situation before the Territorial authorities in one way and has treated it before the Federal authorities in another. May I suggest that as far as Mr. Camp is concerned this objection be sustained for the time being, and then upon the Territory's

(Testimony of H. W. Camp.)

case they can present any facts and figures they want, and then it will come directly before the Board, whether or not they want to rule on this Federal question, and as far as we are concerned, if the Board wants to go into it at that time, we will not object. Can we not have the matter go on at this time without the Board coming to a definite conclusion as to what it will do on this subject, but simply abate the examination of this subject now. Let the matter be resumed if upon the Territory's main case this Board decides it will be glad to go into this entire [105] Federal question. The only thing, we do not want to pass unchallenged any imputation, and that is all it amounts to, any purpose to show that this witness has not acted bona fide in making the returns he did to the Territorial tax officials.

Mr. KAY: I don't recall having made any imputation whatever. It has not been the Board that has exhibited any reluctance to go into this subject, it is counsel. I submit that under the law providing that these hearings are of an informal nature it is the duty of the Board to hear all evidence that may bear upon these questions. The Board has been very lenient to date in admitting all evidence. We would certainly object to any action of the Board in refusing to entertain this evidence.

The CHAIRMAN: Objection overruled.

Mr. PETERS: May it be understood that our objection applies to all this line of examination?

(Testimony of H. W. Camp.)

Mr. WALSH: Certainly. I might say we have a rule here that all formalities are supposed to be omitted as to objections and exceptions.

(Question read by the reporter as follows:

“Will you state whether or not the document I hand you is a true copy of the Federal income tax return made out by you for E. J. Lord for the year 1930?”)

A. That is a true copy of the original return [106] filed by the taxpayer, signed by myself. It is not a copy, however, of the amended return filed for this taxpayer, and that will explain the difference in the figures shown in connection with this transaction and the figures reported on the Territorial return. Unfortunately we don't have a copy of the supplemental Federal return which was filed.

Q. This return was sworn to by you before a Notary Public?

A. It was.

Q. On the back of this return, under Schedule D, will you state what you have entered?

Mr. WRENN: I object to any examination on this return until we get the final return. This shows the error of permitting this kind of evidence.

Mr. ADAMS: I think if there was a supplemental return that should be examined on.

Mr. KAY: I am examining the witness as to an entry made on this return. I think I should be allowed to examine him on it. I think the Board should allow me latitude in making this inquiry.

(Testimony of H. W. Camp.)

Mr. ADAMS: If there was a supplemental return, I think we are filling up the record unnecessarily.

Mr. WALSH: Well, this is a return made by him and I think he should be allowed to examine on it.

Mr. WRENN: This question indicates the real vice [107] of this examination. This cannot lead you anywhere except to confuse the issues.

Mr. KAY: May I state that again, referring to the provisions of the law as to informal hearings. This is not a court of law and I think the Board should allow any evidence that we may have in relation to the issue.

Mr. ADAMS: I think the supplementary return is the one you should examine him on.

Mr. KAY: We may inquire on the supplemental return. We have to start somewhere.

The CHAIRMAN: Objection overruled. Go ahead.

Q. (Question read by the reporter as follows:

“On the back of this return, under Schedule D, will you state what you have entered?”)

A. Schedule D indicates the disposal of 600 shares of E. J. Lord, Limited, stock by the taxpayer, acquired in 1926, disposed of in 1930; amount realized \$599,743.20; cost \$60,000; subsequent charges, \$1,650. That item was legal expense contracted by the taxpayer. Net gain or loss, \$538,093.20. As I say, those figures have been changed in an amended

return which was filed in similar fashion to the change in figures that was made on the Territorial income tax return. The changed items were identically the same in both cases, and the Assessor has full information regarding the change. I would like to state—— [108]

Mr. KAY: Never mind. You have answered the question.

Mr. PETERS: What were you about to say?

Mr. KAY: I submit the witness has answered the question.

The WITNESS: It may develop later. Mr. Kay may ask that question later.

Q. This sale of 600 shares of E. J. Lord, Limited is the same transaction as the subject of inquiry in this case, is that correct?

A. I don't consider it as a sale under Federal law. I consider it as liquidating dividends, which is specifically required to be reported as a gain subject to tax. It is reported as a capital gain on the Federal return, because the Federal law does not require a liquidating dividend to be so reported, but permits the taxpayer, at his option, to consider it as a capital net gain subject to 12½ per cent tax only, and not subject to surtax.

Q. This transaction reported here in this return is the same transaction that is the subject of inquiry in this case?

A. That is correct.

Mr. KAY: We offer this in evidence.

(Testimony of H. W. Camp.)

Mr. WRENN: Objected to, as it is not the final return.

Mr. KAY: We can come to that later return later.

Mr. ADAMS: Why cumber up the record with something [109] that is not relevant?

Mr. KAY: Mr. Adams was not present yesterday, but we did have some forty exhibits introduced by the taxpayer. This is our first exhibit.

Mr. WRENN: That is a very unusual ground for the admissibility of anything in evidence.

Mr. ADAMS: Why not introduce the return on which the taxpayer paid an income tax. He didn't pay it on this. He paid it on his amended returns, did he not?

Q. Was the first installment of the Federal tax paid on the amount shown here in this return?

A. It was.

Mr. ADAMS: That doesn't answer my objection, however.

The CHAIRMAN: Objection overruled.

(Document offered in evidence received and marked: "Tax Assessor's Exhibit "A.")*

(Recess.)

Q. From an accounting standpoint what is surplus considered as? Is it considered as capital or considered as something else?

A. Ordinarily surplus, if the title of the account be "surplus" it is looked upon as indicating accumulated profits of the company which are available for

*Omitted from printed record on stipulation by counsel.

(Testimony of H. W. Camp.) •

distribution as dividends. If the caption of the account is "Capital surplus" it [110] indicates that the balance of that account was due generally to contributed surplus, contributed capital at the inception of the company, or inception of the company or business by some transfer to that account of other items than profits of the company.

Q. When earnings are plowed back to a company and go into surplus account they are considered, are they not, as capital?

A. The proportion of those earnings that are plowed back into the company,—the term "plowed back" must mean from an accountant's viewpoint, that the earnings have either been invested in plant or used for operating expenses or in ways other than in distribution of dividends to stockholders.

Q. Is "surplus" confused with the term "working capital"?

A. I don't quite understand your question. Would you mind illustrating in a concrete way what you mean?

Q. Do you know of any instance where surplus has ever been confused, as a matter of terminology, with the working capital?

A. I don't quite understand what you mean by "confused." You mean that surplus is looked upon as working capital?

Q. We will take that construction. Has it ever been looked upon as working capital?

A. Yes, I should think so. [111]

(Testimony of H. W. Camp.)

Q. In 1929 when E. J. Lord, Limited, purchased the 600 shares of stock from E. J. Lord, what account was debited?

A. I can't answer that question. I am not familiar with the opening entries of the books of the corporation at its inception.

Q. Wasn't the treasury account debited?

Mr. PETERS: There is no treasury account. There was some entry as to treasury stock.

A. I think Mr. Buchholtz can answer that question better than I. I am not familiar with the opening entries of the corporation.

Q. Have you any of the balance sheets of the corporation here?

A. No. I think not. I have no balance sheets. The corporation exhibits previously filed would give the complete balance sheets for each year,—filed as exhibits yesterday.

Mr. WRENN: The ones filed with the Treasurer?

A. Yes.

Mr. KAY: I call upon the Taxpayer at this time to produce trial balances for the months January to December, 1930, inclusive; also November and December of 1929. Could those be produced?

Q. Did you have anything to do with the appraisal and net worth of the corporation?

A. I did not.

Redirect Examination [112]

By Heaton L. Wrenn, Esq.

Q. You were put on your cross-examination a hypothetical question by Mr. Kay having to do with

(Testimony of H. W. Camp.)

the sale of Eqa Plantation stock. Mr. Kay spoke of a capital gain in his question. Do you recall any case where they speak of a capital gain?

A. Not in the Territorial law. They speak of a gain. They do not speak of a capital gain.

Q. Will you explain to us what is the difference between the sale of a corporation exchanged between two individuals and the redemption of stock by a corporation, as we have in this case?

A. I consider the two transactions entirely different. A sale of stock by one stockholder to another, as Mr. Kay spoke of, would not affect the accounts of the corporation whatever. There would be no distribution of surplus, no change in the surplus or profit and loss account of the corporation whatsoever; no change in its capital stock account. The outstanding shares would remain the same after the transaction as they were before. The share of the earnings which the stockholder might claim as being entitled to because of his ownership of stock in the company would ride with that stock when the new stockholder acquires that stock. In the case of the disposal of stock owned by a stockholder to a corporation for the purpose of redemption we have an entirely different situation in that case. And I would like to mention here that the [113] redemption of capital stock by a corporation is nothing new in accounting. Dickenson, an eminent English accounting authority, has quite a section in his book on "Accounting Procedure," I believe it is, (I have the book here), setting forth the procedure of

(Testimony of H. W. Camp.)

accounting where capital stock is redeemed. Saliers, an American authority, also covers that subject, and Kester in his volume 2 (I have the title over here but I can't give it at the present time; it is very familiar to all accountants), set forth the way capital stock is redeemed, and all these authorities discuss the effect on a corporation's books in case the stock of one or more of the stockholders may be redeemed. All of them agree that the action of redeeming the stock naturally must result in a change in the capital stock of the company, providing the stock is surrendered and cancelled, and they also show that the interest of the remaining stockholders may be affected. That is to say, their share and interest in the surplus and undivided profits account is directly affected in case that stock is redeemed at a figure other than the par value of the stock, and also providing the payment to the stockholder whose stock is turned in for redemption is not in exact accordance with the proportion of that stockholder's interest in the undivided profits or surplus as indicated by his [114] stockholdings. I believe that sets forth in brief the extreme difference between a sale of stock by one stockholder to another, and the disposition of stock to a corporation for purpose of redemption.

Q. You are familiar with the provisions of the contract of December 13, 1929, are you not?

A. Yes.

Q. And in making up your returns based upon your familiarity with this transaction you con-

(Testimony of H. W. Camp.)

sidered it as a dividend within the meaning of section 1308, revised laws, did you not?

A. That is correct.

Q. You were present when Mr. Kay was stating to the Board the method of taxation of liquidating dividends under the Federal tax laws?

A. Yes.

Q. And you heard the statement he made in regard to how these were taxed?

A. I did.

Q. Will you explain to the Board the condition of the Federal law in this regard, your knowledge of it?

A. Under Federal law a liquidating dividend is considered as resulting in a gain or loss, taxable or deductible, as the case may be, to the stockholders, but the stockholder is not required, under Federal law, to report such gain under Schedule D, [115] which is known as the capital net gain or loss from sale of assets, on the Federal return. As I recall Mr. Kay's statement in that connection, he stated that the Federal law required the taxpayer to report the gain or loss from a liquidating dividend as a capital net gain under this Schedule D. That is not my understanding of the Federal law. I understand that the taxpayer may at his option so report the gain or loss from a liquidating dividend and thereby be subjected to 12½ per cent. tax, but that it is not obligatory for him to do so. He may treat it as subject to sur-tax. I might add may treat it as subject to sur-tax and the normal tax.

(Testimony of H. W. Camp.)

Mr. ADAMS: You mean if he returned it as liquidating dividend it would be subject to normal tax and subject to the sur-tax also?

A. Yes, but he has the option of reporting it as a capital gain if he desires to do so. If his combined sur-tax and normal tax is less than $12\frac{1}{2}$ per cent. he would not do so.

Mr. ADAMS: In other words, you assume the taxpayer in returning his income and in computing the tax that he would return it as a liquidating dividend if it computed at less than $12\frac{1}{2}$ per cent., and, if it computed at more than $12\frac{1}{2}$ per cent. he would return it as a capital net gain?

A. No. I do not mean that. In either case he reports [116] it as a liquidating dividend, but he may report it as under the capital net gain provision. He may report a liquidating dividend as subject to the normal and sur-tax, if the resulting tax would be less than $12\frac{1}{2}$ per cent.; and if it would be more, he may at his option report it under the capital net gain provision as subject to $12\frac{1}{2}$ per cent. tax only. It is so reported as liquidating dividend in either case. Where a stockholder is paid his proportion of the undivided profits and surplus or capital of the company in the nature of a liquidating dividend, I consider it must come under the provisions of the Federal law relative to liquidating dividends and that such a transaction is not exactly the same as the sale of stock from one stockholder to another.

(Testimony of H. W. Camp.)

Q. The condition of the Federal law you have testified to is the Federal law that has existed since 1926?

A. Yes, the 1926 and 1928 Acts are quite the same in that particular respect.

Q. Is not this the case, that the Federal income tax law does not in any way seek to change the character of a liquidating dividend, but merely permits you to treat it as capital gain for taxation purposes?

A. Yes. [117]

Q. What was the situation under the Federal law in regard to liquidating dividends prior to the change made in 1926?

A. There have been quite a number of changes in prior acts. At one time they were taxed as ordinary dividends.

Q. Even when the law said "Gains from all other sources" they were taxed as ordinary dividends?

A. There was a specific provision that liquidating dividends should be taxed as ordinary dividends and subjected to the sur-tax.

Q. In connection with your explanation of the Federal income tax laws, I call your attention to Article 624 of regulation 74, Federal income tax regulations. I would like to have you read that.

A. I am reading from regulation 74 issued by the Treasury department relative to the Revenue Act of 1928. This is the Treasury department regu-

(Testimony of H. W. Camp.)

lations governing the Federal income tax law. "Article 625". Headed "Distribution in liquidation": "Amounts distributed in complete liquidation of a corporation are to be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation are to be treated as in part or full payment in exchange for the stock so cancelled or redeemed." The phrase "amounts distributed in partial liquidation" means a distribution of a corporation in complete cancellation or [118] redemption of a part of its stock, or one of a series of distribution in complete cancellation or redemption of all or a portion of its stock. A complete cancellation or redemption of a part of the corporate stock may be accomplished, for example, by the complete retirement of all the shares or a particular preference or series or by taking up all of the shares of a particular preference or series and issuing new shares to replace a portion thereof, or by the complete retirement of any part of the stock whether or not pro rata among the stockholders." That is the section of that article which I would like to place before you for consideration. I will read one more paragraph: "The gain or loss to a shareholder from distribution in liquidation is to be determined as provided in Section 111, Article 561, by comparing the amount of distribution with the cost or other basis of the stock, provided in Section 113, Articles 591 to 604, but the gain or loss will be recognized only to the extent

(Testimony of H. W. Camp.)

provided in Section 112, and Articles 571 to 580. Any gain to the shareholder may at his option be taxed as a capital net gain in the manner and subject to the conditions prescribed in Section 101 and Articles 501 to 503''. I will not read further, because this article goes on to cite certain examples, and has reference to distributions [119] in case of reorganization which I consider does not bear on the case. I would like to point out that this resolution speaks of the redemption of capital stock, either partially or in full, in complete retirement of one shareholders stock or more than one.

Q. Does the regulation which you have just read in the Federal income tax act apply to voluntary as well as involuntary redemptions of stock?

A. Yes, I should say so.

Recross Examination by Harold T. Kay, Esq.

Q. In your opinion this payment made by E. J. Lord, Limited, To E. J. Lord, was not a capital net gain but was a liquidating dividend?

A. Yes. In viewing it from Section 1391 I believe it is. In the Territorial law it is a liquidating dividend, the same under Federal law also.

Q. Have we any such term in our Territorial law as "liquidating dividend"?

A. No, not that I know of.

Q. We do tax capital net gains under our law?

A. You tax gains and profits.

Q. In 1390 there is a provision that all gains from the sale of moveable property are taxable?

(Testimony of H. W. Camp.)

A. The law will speak for itself on that. I think that is so. I don't know the exact wording of the law, but in general gains from sale of assets from [120] one individual to another, or one corporation to another, are subject to tax, providing there is a profit on them, and where they do not involve the distribution of undivided profits to the stockholder.

Q. Under the Federal law is it not a fact that the terms "Liquidating dividends" and "Sale of capital assets" are used synonymously to represent the same thing?

A. I would not say that.

Mr. PETERS: I object to that. It seems to me we are getting into the realm of speculation here, asking the witness to determine those things which the Board will be ultimately called upon to determine. As far as we are concerned, if the Board feels that these references to the Federal law are material, we have no objection, but to ask the witness what construction he puts on the terms in the different laws seems to me is asking the witness to put construction on things which it is the province of the Board to determine. As a matter of fact, as to whether or not a liquidating dividend is the same dividend under the Territorial law is another question for the Board to decide, and, obviously, that Board can conceive right now of liquidating dividends in some instance containing capital, but when the liquidation comes in partial liquidation of stock it may also contain capital, [121] and under the law

(Testimony of H. W. Camp.)

it does not make any difference in the Federal law, but under the Territorial law you must deduct the portion that is capital and it only applies to what it apparently profits, in dividends.

Mr. ADAMS: The witness is qualified as an expert accountant.

Mr. PETERS: If it is just from an accountancy standpoint I have no objection.

Mr. ADAMS: And one who is qualified to make Federal returns.

Mr. PETERS: If it is from that standpoint, as to whether or not it is from an accountancy standpoint, the objection is not well taken.

Q. (Question read by the reporter as follows: "Under the Federal law is it not a fact that the terms "Liquidating dividends" and "Sale of capital assets" are used synonymously to represent the same thing?)"

A. My answer was incomplete owing to the objection taken at that time. I would not say so, for this reason: My understanding of the Federal law is that liquidating dividends and any resulting gain from such liquidating dividends to the taxpayer, must, under Federal law, be returned,—the gain must be reported the same as if the stockholder had sold his stock. That is my understanding of the [122] Federal requirements. The Federal law does not say, however, that a liquidating dividend is a sale of stock. It merely requires that the stockholder reports his gain or loss from that transaction

(Testimony of H. W. Camp.)

in the same way as if he disposed of his stock in some other way, than obtaining his distribution from the surplus of the company. Does that answer your question, Mr. Kay?

Q. Not quite. Doesn't a liquidating dividend represent a distribution of assets?

A. It must. If the company pays out cash it is bound to.

Q. And the gain on that distribution is measured by the price paid and the value distributed, isn't that correct?

A. Under Federal law there are a good many provisions affecting the determination of that question. First of all it depends on when the stock was acquired, how it was acquired, whether it was acquired prior to August 1, 1913, or subsequent thereto, whether it was acquired by gift prior to December 31, 1920, or subsequent thereto. It further depends on whether or not the corporation has issued any distributions which are not subject to tax under Federal law, any partial liquidating dividends which may have been declared between the time the stockholder acquired his stock and the time he received his final distribution must [123] have the effect of reducing the cost.

Q. In any event, the gain is measured by the cost to the stockholder of his stock and the value of the distribution to him?

A. I would qualify that by saying that the cost, as governed by the provisions of the Federal tax

(Testimony of H. W. Camp.)

law, the cost as determined under Federal law, not the exact cost to the taxpayer in dollars and cents.

Q. We will say the basis of the cost, then?

A. Will you give that question again, please.

Q. (Question read by the reporter)

A. Yes.

Q. And that gain is not considered as a taxable dividend under Federal law, is it?

A. Yes, it is considered as a liquidating dividend subject to tax.

Q. Isn't it—a liquidating dividend—used in a different sense from that of the regular taxable dividend declared by a corporation in its usual course of business from net profits?

Mr. PETERS: That is what we have been contending for right along.

Mr. WALSH: Let him answer the question.

A. I would like to have the question read again.

Q. (Question read by the reporter)

A. A liquidating dividend is a regular taxable dividend. I cannot see we can divide,—there is nothing [124] I understand in the Federal law that speaks of a regular taxable dividend on one hand and a regular liquidating dividend on the other. They are both taxable dividends.

Q. Where is the term liquidating dividend usually used for the purpose of making out tax returns?

A. It applies to situations such as I read from the regulations, article 625, a moment ago. Where

(Testimony of H. W. Camp.)

there is a partial distribution of the company's assets in redemption of a part or all of stockholders' stock that liquidating dividend may be paid out of surplus; it may be only a partial distribution. If it is paid out of certain reserves the Federal law permits a distribution out of certain reserves in such a way that they shall not be subject to Federal income tax. You may have liquidating dividends in that sort of situation.

Q. Essentially, however, a liquidating dividend is a distribution of assets?

A. It is a distribution of assets purchased out of accumulated earnings of the corporation,—assets which have resulted from plowing in of profits of the corporation.

Q. Can liquidated dividend be made from capital?

A. Yes, then you have a situation of reducing the capital stock. When you say "capital" I assume you mean out of capital stock resulting in reduction of capital stock and returning to the taxpayer his [125] par value of the investment.

Q. So any distribution may be considered a liquidating dividend?

A. No, not in Federal law or Territorial law. A cash distribution reduces the surplus, but it is not a liquidating dividend.

Q. Are you familiar with Prentiss-Hall "Federal Cumulative Tax Service" volume 2 of the Edition of 1929?

(Testimony of H. W. Camp.)

A. I am not, but I am familiar with the Corporation Clearing House Service and the two services are very similar.

Q. Referring to volume 2 of this service, page 9051, section 115, article 629, entitled "Distributions", being the Federal regulations, and examples thereunder, the following is said: "On the other hand, a cancellation or redemption by a corporation of all the stock of a particular shareholder so the shareholder ceases to be interested in the affairs of the corporation does not effect the distribution of a taxable dividend". Will you state whether or not that statement conforms to your idea in respect to that matter?

A. I will state that that section of Article 629 specifically mentions that where the distribution and cancellation or redemption in whole or in part is essentially equivalent to the distribution of a taxable dividend, then the amount so distributed [126] in redemption or cancellation of the stock shall be treated as a taxable dividend. I quite agree with that, but I should like to point out that is only in those situations where the distribution is essentially equivalent to the distribution of the taxable dividend, and if Mr. Kay will look in Prentiss-Hall in the second paragraph he will find this statement: "On the other hand, a cancellation or redemption by a corporation of all the stock of a particular shareholder, so the shareholder ceased to be in-

(Testimony of H. W. Camp.)

terested in the affairs of the corporation, does not affect the distribution of a taxable dividend."

Mr. WALSH: That is the question he asks you.

A. In that particular situation the Federal law goes on to subject the liquidating dividend to the tax as a liquidating dividend.

Q. And that tax cannot be less than the tax on capital net gain, can it?

A. Yes, certainly.

Q. Is it not provided in the Federal law it cannot be less?

A. No, the capital net gain is optional to the taxpayer. It is an optional provision, as I understand it. The taxpayer does not have to report the gain from the disposal of any asset there in any way whatever. He is not required to report it as a [127] capital net gain subject to the 12½ per cent. tax.

Mr. ADAMS: You mean if you treat it as dividend, it is subject to the normal tax and surtax, if the tax is less than 12½ per cent. then you don't have to report it as a capital net gain?

A. That is my understanding.

Mr. ADAMS: So he need not report it as a capital gain?

A. That is my understanding.

Q. In your Federal income tax return if the Federal law would have required a less tax why

(Testimony of H. W. Camp.)

would not this gain be reported as a liquidating dividend?

A. This transaction was reported as liquidating dividend. The taxpayer through his agent choose to elect that gain be taxed under the capital net gain tax rate which is $12\frac{1}{2}$ per cent. That is the very situation covered by this article. It permits the taxpayer, if he would be taxed a greater amount than under the normal and sur-tax rates it is not classed as an ordinary taxable dividend, but it may be considered as a transaction that he may at his option select to be taxed $12\frac{1}{2}$ per cent. Necessarily the taxpayer would not select that option to be taxed under the capital net gain provision nor would he have paid it under section "D" if he had reported it subject to the normal and sur-tax rates. [128]

Mr. PETERS: Let me understand it. May I ask the witness a question to clear it up?

Mr. KAY: There are two or three questions I would like to ask in connection with the witness.

Mr. PETERS: I don't understand the answer of the witness at all. Perhaps your questions will clarify that question.

Q. Unless this transaction were within the class of capital net gain transactions it could not have been reported as a capital net gain transaction, could it?

A. The regulations provide that this particular kind of a transaction may be reported as a capital net gain.

(Testimony of H. W. Camp.)

Q. In other words, they consider that type of transaction as within the class of capital net gain transactions, that is correct, is it not?

A. That is my understanding of the law. They don't limit it to a capital net gain. A capital net gain transaction is one where a taxpayer disposes of capital assets which he has held for more than two years prior to date of sale. It is purely an optional provision in the law and the taxpayer does not have to report his transaction as a capital net gain. He simply reports the gain as subject to tax. He must report it subject to tax, but not necessarily as a capital net gain. The law requires him to report the gain and the liquidating dividend, measured [129] by the difference between the cost basis and the amount received in liquidation. That is classified as a taxable gain. As far as the taxpayer is concerned, he may report it in any way he likes on his tax return, but the regulations specifically provide, article 629, specifically provides that where a corporation distributes amounts to a taxpayer in full or partial liquidation of his stock,—I don't mean partial liquidation, I mean in complete retirement of his stock—that consideration shall not be construed as a taxable dividend, therefore that provision enables,—and if it were not for that provision the taxpayer could not possibly take advantage of the capital net gain of 12½ per cent.,—but that provision specifically enables him to report that net gain under the capital net gain tax rate.

(Testimony of H. W. Camp.)

Q. Under the Federal law a liquidating dividend may entitle the taxpayer to claim a loss, may it not?

A. Yes.

Q. Do you know of any provision in our law that contemplates or considers any dividend paid by a corporation of the nature or having the nature of a loss to the recipient?

A. No, I don't know of any provision allowing a loss to the recipient. In a case of that kind our law is not very specific. In the matter of dividends it does not specify the difference between ordinary [130] dividends and liquidating dividends, or dividends declared from depreciation, depletion or depletion reserve.

Q. Are you familiar with section 1361, Revised Laws of Hawaii, providing for the duties of managers of corporations. Will you examine that and state whether or not you are familiar with that provision?

Mr. WRENN: I object to getting off on this other angle of this case. That is a section on corporations that has to do with the liability of directors to declare dividends, which may impair the assets of the corporations. This has nothing to do with any of the issues before the Board. That is something a tax man is not interested in.

The CHAIRMAN: Objection sustained.

(Adjourned to 9 o'clock a.m., Monday, December 7, 1931.) [131]

(Testimony of H. W. Camp.)

[Title of Court and Cause.]

The above entitled matter came duly on for further hearing before the aforesaid Board on Monday, December 7, 1931, at 9:40 o'clock a.m., all Members of the Board and all parties to the hearing being present, and the following further proceedings were had and testimony taken:

Mr. KAY: The Government did not make preparations to go ahead this morning, as I understood this case would not go on this morning. We are willing to accommodate counsel and the Board this morning and go ahead as far as we can, if the Board so desires.

The CHAIRMAN: Go ahead with it.

Mr. WRENN: We should like to go on.

GEORGE BUCHHOLITZ,

a witness for the Taxpayer, resumed the stand and testified as follows:

Cross Examination by Harold T. Kay, Esq.

Q. How long have you been Secretary of E. J. Lord, Limited?

A. Since the time of incorporation.

Q. What is your official title, Mr. Buchholtz?

[132]

A. Treasurer at that time. Now I am Treasurer and Secretary.

(Testimony of George Buchholtz.)

Q. E. J. Lord, Limited, was incorporated back in 1926, was it?

A. Yes.

Q. Who were the stockholders at that time?

A. Time of the incorporation?

Q. Yes.

A. Mr. Lord, Mr. Black, myself, Mr. Ikejiri, and I think Mr. Erbes.

Q. And the stock held by these respective stockholders was how much?

A. Mr. Lord had originally 797 shares, to the best of my recollection. Mr. Black had 200 shares, and these other three had one share each.

Q. How were those shares paid for?

A. Mr. Lord had a certain amount of plant that was turned into the capital, which was valued at—

Mr. PETERS: May I suggest if you consider this material that the witness have the affidavit of the corporation so the exact figures may come to the Board. The entire matter is set forth in the affidavit of the corporation, and according to the evidence of Mr. Buchholtz the figures were compiled by him, so as long as the Board is considering this evidence, it might just as well have it properly before us as otherwise.

Mr. WRENN: I would like to have it stated at this time [133] that this question of the original contribution is not before the Board. Mr. Glass has admitted that the sixty thousand dollars received was equal to his original capital contribution. It is just another phase of the matter that we are not

(Testimony of George Buchholtz.)

concerned with whatever. That is one thing the pleadings admit. I submit we can get nothing that will assist the Board by going into this original contribution, when the figures the Board has and Mr. Glass has admitted that the figures were sixty thousand dollars in making up his original assessment.

Mr. KAY: I submit the question is relevant.

Mr. WRENN: I would like to have a ruling on that by the Board.

The CHAIRMAN: Do you object to the question?

Mr. WRENN: Yes, it is incompetent, irrelevant and immaterial. The facts are admitted.

Mr. ADAMS: This plant, in the articles of incorporation, is valued at sixty thousand dollars?

A. I can't remember those. It is quite a complicated affair. (Referring to affidavit.)

Mr. WRENN: Your question refers now to the time this deal went through?

Mr. ADAMS: Yes.

Mr. WRENN: The question is whether or not his capital contribution was valued at sixty thousand dollars at the time this deal went on? [134]

Mr. WALSH: No, that's not the question.

The WITNESS: What deal?

Mr. PETERS: The option of December, 1929.

A. Mr. Lord had sixty thousand dollars worth of stock at that time.

(Question and answer read.)

(Testimony of George Buchholtz.)

The WITNESS: Had eighty thousand dollars.

The CHAIRMAN: Objection sustained.

Mr. KAY: May it please the Board, we would like to have an understanding at this time as to what—

The CHAIRMAN: As I understand, Mr. Glass had admitted all of these figures.

Mr. KAY: There have been no admissions by Mr. Glass.

Mr. PETERS: He has admitted it in his assessment.

Mr. KAY: This is a matter of cross-examination and we should know what he paid for that stock at that time.

Mr. WRENN: All you have to do is to ask Mr. Glass if he hasn't admitted it in his assessment.

Mr. WALSH: That is immaterial. This document has been admitted in evidence and we have the right to discuss it.

Mr. PETERS: That may be true in a certain sense. I take it that affidavit is not subject to impeachment.

Mr. WALSH: There is no question of impeachment.

Mr. PETERS: If there is no question of impeachment here should this matter be gone into? This is [135] immaterial, because it is all set forth here. The affidavit of incorporation of E. J. Lord, Limited, states who the officers are, the number of shares and the cash that has been paid for three of the shares. Listen to this language:

(Testimony of George Buchholtz.)

“That \$300. has been paid in cash for three of the said shares and it is intended that before the company engages in business that all the personal property hereinafter more particularly described forming and used as a general contracting and engineering business in the Territory of Hawaii, and heretofore carried on under the name ‘E. J. Lord’ will be assigned to the company by said Edmund J. Lord in exchange for 800 shares to be issued to him as fully paid up and non-assessable in exchange for said property, and that a promissory note for the sum of \$20,000. dated July 31, 1926, made by the said Edmund J. Lord payable on demand to said Everett E. Black, without interest, and constituting a debt payable by said business, will be paid by the said Company by issuing to said Everett E. Black 197 shares of said Company, as fully paid up and non-assessable, and by the payment by the Company of \$300 in cash to said Everett E. Black in exchange for said promissory note, which will then be delivered to the Company and cancelled as paid. The object of the incorporation of E. J. Lord, Ltd., is to take over and conduct as a going concern the general contracting and engineering business now carried on in the Territory of Hawaii by the said Edmund J. Lord under the name of ‘E. J. Lord,’ a full description of the property comprising which, and intended to represent 80% of the capital stock of the proposed corporation and

(Testimony of George Buchholtz.)

a detailed valuation of each item of said property is as follows: Assets: Accounts Receivable" so much; Contracts Receivable; Contracts a/c Reserves; Personal Accounts Receivable; Plans and Specifications; Cash on Hand; Prepaid Insurance; Supplies and Materials; Plant and Equipment; Less Depreciation Reserve; Office Building, Kakaako; Furniture and Fixtures; Auto and Tool Shed; Kakaako; Good Will;" making a total of \$254,997.03. "Less liabilities, etc., \$105,997.03 and Notes Payable, \$69,000.," making \$174,997.03, showing net total of \$80,000. * * * "Also the object of incorporation of said E. J. Lord, Ltd., is to take over and pay the said promissory note for \$20,000. dated July 31, 1926, made by the said Edmund J. Lord payable on demand to the said Everett E. Black or order, said promissory note to be paid by the Company by the issue of stock and \$300. in cash, as stated above." [136]

And then follows the conveyance from Edmund J. Lord to E. J. Lord, Limited. Now we have gone right through, down through the history of the corporation, until we come, as Mr. Wrenn has properly called to the attention of the Board, to the figures as they are contained in the return, and as far as I understand it there has been no objection made by Mr. Glass to the figures as returned by the taxpayer, showing that the capital as represented in the amount received by E. J. Lord in redemption of his stock as sixty thousand dollars.

(Testimony of George Buchholtz.)

Mr. ADAMS: After all these deductions there were assets of eighty thousand dollars, less a promissory note of twenty thousand, which makes sixty thousand dollars, and in this computation by the tax assessor are the figures sixty thousand dollars.

Mr. KAY: I think counsel is anticipating the object of this particular inquiry. It is not to attack the value of the property transferred, but the nature and the character of that property, and as far as the issues are concerned we have no intention to challenge the value of the property. Mr. Glass, it is true, has not challenged the value, to-wit, sixty thousand dollars, but when all this mass of stuff is thrown into evidence, I think 44 exhibits, containing a great deal of data and so forth, data that has not been explained in direct examination, certainly we have the right on cross to inquire [137] into that particular data, the character and nature of it, and if the Board has permitted holus bolus the admission of all this data, I don't think the Board, in fairness to the Government, should refuse an examination into the character and nature of the data.

Mr. PETERS: I don't think there is any question as to the character of this property that was turned in.

Mr. WALSH: Why not let the witness answer that question. You have answered it twice, but why not let the witness answer it.

Mr. WRENN: My point is that at the last hearing we objected to going into the question of Federal

(Testimony of George Buchholtz.)

income tax and we spent two days on it. Now we may spend two days on this.

Mr. KAY: I haven't heard a statement of the issues made by opposing counsel to this Board.

Mr. WALSH: We will assume the issues by reading the appeal, but counsel haven't announced the issues.

Q. Included among this property turned over by Mr. Lord there were various contracts, were there not?

Mr. WRENN: Same objection.

Mr. PETERS: You are speaking now of 1926?

Mr. KAY: Yes.

Mr. ADAMS: I think we are wasting a lot of time. It is all set forth in the affidavit and it is boiled down in the tax assessor's admission of eighty [138] thousand dollars. It all boils down to eighty thousand dollars, less the promissory note for twenty thousand dollars, which gives sixty thousand as the value of the stock.

Mr. KAY: I do not desire to unnecessarily prolong the subject of inquiry. I think I could dispose of it in about two minutes. I might state that in direct examination counsel has gone to considerable extent in endeavoring to build up the fact that only earnings have gone into this surplus account from which they contend payment was made to Mr. Lord. They have gone into the history of the corporation, the financial set-up and the character of the various accounts. I think we are perfectly proper in making inquiry into the origin of the property of the cor-

(Testimony of George Buchholtz.)

poration. If the Board does not care to have us proceed along that line, we will defer to the wishes of the Board. If the Board does not feel it is relevant, we do not desire to unnecessarily take up the time.

Mr. WRENN: If Mr. Kay will make an offer of proof that any of the \$468,000. distributed to Mr. Lord is capital, I will withdraw any objection, but I do object to his going on a fishing expedition when it will serve no good purpose. Mr. Glass has taken the amount of capital as sixty thousand dollars. The only question is whether the difference between [139] the sixty thousand dollars and the \$468,000. was an amount on which an income tax has been paid. That is the only difference between his assessment and the return which was made by the taxpayer.

The CHAIRMAN: Objection sustained.

Mr. KAY: May we have our objection to the ruling of the Board.

Q. Turning to Taxpayer's Exhibit 34 for the year 1926 is any of that income there noted under the column of 1926 derived from the contracts assigned by Mr. E. J. Lord to E. J. Lord, Limited?

A. I will have to look that up. I don't know whether any contracts went over or not. I can't remember that off-hand.

Mr. PETERS: Do I understand from your question that the contracts are considered by you as capital gain and hence not income? Otherwise, it seems to me, if the Board please, that this question

(Testimony of George Buchholtz.)

is objectionable on the same ground as raised by Mr. Wrenn. I think the position of the taxpayer should affirmatively appear on the record that if there is any item, offer or proof of which Mr. Kay desires to make, contained in the surplus account that is not surplus profits, but, on the other hand, is capital, we are willing to meet that issue, but, in the absence of any offer to meet that issue it seems to me it comes within the objection we raised.

Mr. KAY: Is the Board going to proceed along the [140] lines already adopted by it, to-wit, informal proceedings, allowing parties to make objections and take exceptions and proceed, or allow these objections to be made and refuse counsel to inquire into the subject matter already presented by opposite counsel.

Mr. ADAMS: I don't think that question is objectionable.

Q. Will you make an examination of your books?

A. I can answer that question now. There were certain contracts taken over from E. J. Lord to E. J. Lord, Limited. They were closed up entirely up to that date and any profits or losses on those contracts went into profit and loss.

Q. In what year would those profits appear, if any?

A. 1926.

Q. Were there any profits made on those contracts in 1927?

A. I think they were all completed in 1926. I am not positive of that, but I think they were all completed.

(Testimony of George Buchholtz.)

Q. Will you make an examination before our next hearing and be prepared to state whether or not they were all closed out in 1926? Now, in 1926, 1927 and 1928 dividends were declared by your corporation, were they?

A. Yes. [141]

Q. How were those dividends declared?

A. How they were declared?

Q. Yes, what was the procedure?

A. The minutes show they were authorized to be paid in the meetings.

Q. What were the proceedings in these meetings?

A. Declaration of dividends from the surplus.

Q. Was that declaration duly noted in the minutes?

A. Yes, sir.

Q. Have you got a form of the usual declaration of dividend as contained in your minutes?

A. The regular form? No, the meetings were called at different times to declare the dividends. There was no regular form.

Q. It would appear in the minutes?

A. Yes.

Q. And that dividend would be payable to the stockholders according to the amount of stock held by them?

A. Yes.

Q. At the time of this agreement with Mr. Lord in 1929 was there any declaration of dividends?

A. I haven't quite got your question. In what time in 1929?

(Testimony of George Buchholtz.)

Q. Any time in 1929?

A. I think there were dividends declared in 1929, yes. The statements here will show that. May I look [142] at that dividend and surplus account for a minute. (Witness examines paper) 1929,—yes, dividends were declared.

Mr. WALSH: How much?

A. On March 31st \$30,000.; April, \$50,000.; May, \$70,000.; total \$150,000.

Mr. WALSH: March, April and May.

Q. Does the payment to Mr. Lord appear in the minutes as a dividend declared by the corporation in 1930?

A. It does not appear.

Mr. PETERS: We will admit it appears as a redemption of stock.

Q. Let the witness answer that.

A. I will have to examine again. (Witness examines papers) Mr. Lord did not receive any dividend in 1930. \$25,000, was paid to Mr. Black. Are you referring to liquidating dividends?

Q. No, I am referring to dividends.

A. There were \$25,000. paid to Mr. Black.

Q. So that in the year 1930 the only dividend declared was a dividend of \$25,000?

A. Only regular dividend.

Mr. WALSH: Was there any special dividend?

A. There was a liquidating dividend paid.

Mr. WALSH: Declared?

A. Declared. [143]

(Testimony of George Buchholtz.)

Q. In the year 1930?

A. No, it was paid in 1931, I guess.

Q. There was no dividend declared in 1930?

A. That \$25,000. was declared.

Q. That was the only dividend of any character whatsoever declared in the year 1930?

A. Yes.

Mr. KAY: May it please the Court, counsel has introduced a great mass of material here, that I haven't had an opportunity of examining fully, and I would like to have the privilege of deferring further cross-examination of this witness until our next hearing, assuming I feel it necessary, giving me an opportunity of completing my examination of all these exhibits. The Board will recall that a lot of these exhibits were introduced without objection on our part, subject, however, to my examination. We haven't had an opportunity to make a full examination.

The CHAIRMAN: There is no objection to that.

Mr. PETERS: We understand that our redirect examination of Mr. Buchholtz is left entirely open. This matter of dividends that has been gone into this morning, we should like to go into that.

Mr. WRENN: We will reserve that on our full redirect-examination when he is through with cross.

(Witness withdrawn.)

Mr. WRENN: I offer in evidence minutes special meeting [144] of the Board of Directors of

(Testimony of George Buchholtz.)

E. J. Black, Limited, held at the office on December 5, 1930, at 11 o'clock a. m.

(Document offered in evidence received and marked: "Taxpayer's Exhibit 37D.")

TAXPAYER'S EXHIBIT 37-D

MINUTES of a Special Meeting of the Board of Directors of E. E. Black, Ltd., held at the office of the company on December 5th, 1930 at 11 A. M.

PRESENT:

Mr. E. E. Black, President
" Geo. Buchholtz, Treasurer
" T. Ikejiri, Secretary

CHAIRMAN:

There being a quorum present, Mr. Black took the chair and called the meeting to order.

MINUTES OF AUGUST 13th, 1930:

The minutes of a Special meeting of August 13th, 1930 were read, approved and ordered placed on file.

ADDITIONAL PAYMENT FOR PLANT TO MR. E. J. LORD:

Mr. Black stated that Mr. Lord for some time past had been requesting an additional sum of over \$12,000.00 for Plant in the first part of his settlement, on account of there being items of Plant in existence, which were not shown in the Plant Account, and whereas Mr. Lord was willing to compromise for the sum

(Testimony of George Buchholtz.)

of \$3,500.00 suggested acceptance. Mr. Buchholtz moved that the offer to compromise for \$3,500.00 be accepted and paid at the time of the final settlement, Mr. Black seconded the motion, carried unanimously.

ADJOURNMENT:

There being no further business the meeting adjourned.

(Sgd.) T. IKEJIRI,
Secretary. [313]

Mr. KAY: May this offer carry our reservation also of examination.

The CHAIRMAN: Yes.

E. E. BLACK

was duly called and sworn as a witness for the Taxpayer, and testified as follows:

Direct Examination by Heaton L. Wrenn, Esq.

Q. You are E. E. Black?

A. I am.

Q. You own all the capital stock of E. E. Black, Ltd.?

A. I do.

Q. Formerly you owned 40 per cent. of the stock of E. J. Lord, Limited?

A. Yes.

(Testimony of E. E. Black.)

Q. You are not a tax expert, are you?

A. No.

Q. Nor are you an accountant?

A. No, and I am not an attorney either.

Q. You are just a common garden variety of engineer?

Q. In the early part of December, 1929, E. J. Lord, [145] Limited, had certain negotiations with Mr. E. J. Lord relative to his retiring from business, did they not?

A. Yes.

Q. Was it the intention of E. J. Lord, Limited, at that time, when the deal was finally consummated by the preparation of an option on December 13, 1929, to redeem the capital stock held by Mr. E. J. Lord?

A. It was, because it was representing my ambition of a life-time to own my own company.

Q. And the idea was then to pay Mr. Lord in the matter of the redemption of his stock his capital contribution plus his share of the earnings in the company?

A. That is quite right, and the contracts pending.

Q. And after his stock had been redeemed, to retire it and reduce the capitalization to equal the 400 shares you owned in the company?

A. That is quite right.

Q. And further to change the name of the company to E. E. Black, Limited?

A. Yes.

(Testimony of E. E. Black.)

Q. And after the capital stock had been fully redeemed by paying Mr. Lord his sixty thousand dollars and his share of the profits as well as his share of the contracts completed in the year 1930, the capital stock of E. E. Black, Limited, was then [146] reduced, was it not?

A. Yes.

Q. At the time that Mr. Lord owned his stock in E. J. Lord, Limited, you and he were the only real stockholders in the company?

A. Yes.

Q. And the other three persons who held a share of stock apiece held it merely nominally and were dummies?

A. Yes.

Cross Examination by Harold T. Kay, Esq.

Q. Prior to the incorporation of E. J. Lord, Limited, you and Mr. Lord were partners, were you not?

A. No, I worked for Mr. Lord on a salary and a percentage of profits.

Q. And when E. J. Lord, Limited, was incorporated Mr. Lord transferred to E. J. Lord, Limited, the entire business carried on by him?

A. Yes.

Q. And he received in payment of that approximately 800 shares?

A. I can't tell you the exact details of that. It finally worked down to his owning 600 shares and my 400, and part of my 400 was paid off by my percentage of the earnings.

(Testimony of E. E. Black.)

Q. In other words, he owed you money and you turned over to him the particular obligation that he owed [147] you in consideration of his turning over to you a certain amount of stock of E. J. Lord, Limited?

A. Yes.

Q. In other words, you cancelled the obligation he owed you?

A. That is the company.

Q. But it was an individual transaction between the two of you, where he turned over part of his own stock to you, wasn't it?

A. At the very beginning. I think that was only at the beginning.

Q. So the final result was that you owned 400 shares and he owned 600?

A. That's right.

Q. And that relationship in respect to the amount of stock owned by each of you continued until 1929?

A. Yes.

Q. And in 1929 you desired to own your own business and proposed to Mr. Lord to buy him out?

A. That's right. I would not say particularly "buy" because the whole assets of the company were divided 60-40 as best we could. I agreed with Mr. Lord to take the plant, as he was going out of the contracting business, and that value was established, and with the bonds and cash we had that pro-rated 60-40.

(Testimony of E. E. Black.)

Q. In other words, Mr. Lord was contemplating [148] retiring from the contracting business at that time?

A. Yes. It was not a forced sale. Very agreeable.

Q. Might I suggest to you that there was a proposition made that either you buy Mr. Lord out or he buy you out, the two of you couldn't continue on together in the business?

A. No.

Q. Then the proposition was he wanted to get out of the business and wanted to sell to you his interest?

A. Yes. We had had an agreement previously before this was drawn if anything happened to Mr. Lord or to me we would have the first refusal of the stock, and Mr. Lord was not in very good health at that time, and he had at that time more assets than he ever had before in his life, and it was the logical time for him to retire.

Q. So it was proposed that E. J. Lord, Limited, buy Mr. Lord's stock, paying him with assets of E. J. Lord, Limited?

A. I don't know whether you are trying to get technical with me or not?

Q. No, I am not.

A. It was just a division of the assets of the company, plant, stock, bonds and cash, sixty-forty. That is what it amounted to.

Q. In other words, the company would pay to Mr. Lord [149] sixty per cent. of the value of everything the company had?

(Testimony of E. E. Black.)

A. That's right, for the surrender of his stock to E. J. Lord, Limited, which after the first of the year was E. E. Black, Limited, with the understanding that I would take the plant and the stuff, all our legal assets.

Mr. PETERS: When you say "I" you mean E. E. Black, Limited?

A. Yes, E. E. Black, Limited.

(Recess)

Q. I understand from your direct examination, Mr. Black, that this transaction between E. J. Lord, Limited and E. J. Lord, was a transaction whereby E. J. Lord would sell to E. J. Lord, Limited, the 600 shares of stock, and that it was to be paid for by E. J. Lord, Limited, in the assets of the company, and apportioned on a basis of 60 per cent. of net worth and that in your agreement executed in 1929 with Mr. Lord the net worth was to be determined pursuant to amicable arrangements between the parties and that the Territorial and Federal taxes were to be born in the same ratio by E. J. Lord, Limited, and E. J. Lord,—that is to say, 60-40, that is correct?

A. That's correct.

Q. I think you have already made the statement that you are not a tax expert or an attorney or [150] anything but just an engineer, and consequently you left these tax matters and so forth to your legal and tax expert advisors, didn't you?

A. That's quite right. All I do is to take the responsibilities.

(Testimony of E. E. Black.)

Q. And pay them?

A. Yes.

Redirect Examination by Heaton L. Wrenn, Esq.

Q. When you answered several of Mr. Kay's questions you spoke of yourself, what you were to get out of it. You meant what E. J. Lord, Limited, would, didn't you? You personally didn't play any part in this deal?

A. No, only I represented E. J. Lord, Limited.

Q. The deal was between the corporation and Mr. E. J. Lord?

A. That's right.

Q. In regards to the original purchase of your stock before the incorporation of E. J. Lord, Limited in 1926, you actually paid twenty thousand dollars in cold cash out of your pocket, your own pocket?

A. It was cash I had earned.

Q. Whatever you got you paid for yourself?

A. Yes.

Recross Examination by Harold T. Kay, Esq.

Q. E. J. Lord, Limited, at the time of the execution [151] of this agreement with E. J. Lord in 1929 was a going concern, carrying on a general contracting business here in the Territory?

A. Yes.

Q. And there was considerable business on the books at that time too, was there not?

(Testimony of E. E. Black.)

A. Yes, Mr. Lord had a 60 per cent interest in the jobs that extended over the end of 1929. That was part of the agreement.

Q. You had during the years that E. J. Lord Limited had been incorporated and doing business, you had taken a much more active part in the business than Mr. Lord, did you not?

A. I guess you could say that. I was vice president of it, but Mr. Lord left the execution of the work pretty much up to me. He acted pretty much in an advisory capacity. Before that he was in poor health and had family troubles as well.

Q. As a matter of fact, without being too modest, you were responsible largely for the building up of the business of E. J. Lord, Limited?

A. Oh, I would not say that.

Mr. ADAMS: This E. J. Lord, Limited, took over a certain amount of plant and equipment, didn't you?

A. Yes, it was a going contracting concern of E. J. Lord?

Mr. ADAMS: I mean when you negotiated for the retirement of E. J. Lord as an individual you listed [152] a certain amount of plant and equipment as being of a certain value?

A. Yes, we carry that all the time; depreciate it every month.

Mr. ADAMS: Approximately what was that value?

A. Some sixty-five thousand dollars.

Mr. ADAMS: That accounts for the payment, or whatever it may be, retirement of E. J. Lord's

(Testimony of E. E. Black.)

original stock? The value of his original stock was approximately \$60,000. of plant?

A. There had been considerably large plant bought and the original plant was depreciated on book value and some was obsolete and worn-out. This plant account we had then I don't think had any connection with the plant of 1926.

Mr. ADAMS: I don't mean that. As you stated on direct examination, you paid Mr. Lord a certain amount for his share of the plant and equipment of E. J. Lord, Limited, and he was to get 60 per cent. of the profits from the contracts then in existence?

A. Yes, we couldn't arrive at the profit until the job was completed. That's the idea.

Mr. ADAMS: The plant, as I noticed in the minutes of one of the meetings, December 5, 1930, Mr. Lord estimated his own holding, as it were, in the remaining portion of the plant was \$12,000. and you compromised by paying him \$3500.?

A. Yes. [153]

Q. So you did place a value on that plant for which you reimbursed the company?

A. Yes, the plant was valued at something all the time, and the plant Mr. Lord had Mr. Williams appraised, which we thought was high. We worked on the general contractors' schedule, and we had Mr. Grainger of the Iron Works appraise it, and this was worked out as a compromise.

Mr. KAY: What officer of your company has been in charge of tax matters, making returns and so forth?

(Testimony of E. E. Black.)

A. Mr. MacComisky makes out the tax returns, working with Mr. Buchholtz. That is left up to them. They talk to me and tell me what they have done.

Mr. KAY: You will admit as a matter of record that you are representing E. E. Black, Limited?

Mr. PETERS: Yes, I am representing E. E. Black, Limited.

Mr. KAY: And E. E. Black, Limited, under the agreement with E. J. Lord, would be liable for forty per cent. of any Territorial taxes that would have to be paid in this appeal as a result of these proceedings?

A. Yes.

Mr. WRENN: We rest, subject to our right to reexamine Mr. Buchholtz after his further cross-examination.

Mr. KAY: May it please the Board, we would like [154] this matter to go over pending our examination of these documents and other data that have been introduced in evidence. As I stated to the Board this morning, evidently there was a misunderstanding as to this case going on this morning, and consequently we haven't made preparations.

(Adjourned tentatively to Wednesday, December 9, 1931, at 9 a. m. [155])

[Title of Court and Cause.]

The above entitled matter came duly on for further hearing before the aforesaid Board on Satur-

day, December 12, 1931, at 10:25 o'clock a. m., all members of the Board and all parties to the hearing being present, and the following further proceedings were had and testimony taken:

Mr. KAY: We offer on behalf of the Tax Assessor taxpayer's trial balances for the months November and December, of 1929, and for the months of the year 1930, including January to December, inclusive. These trial balances are photostatic copies furnished by the taxpayer as abstracts from the books of the company.

(Document offered in evidence received and marked "Tax Assessor's Exhibit B1 to B14" inclusive.)*

Mr. PETERS: We have no objection unless it is the contention of the Government that these go to show different figures than we have contended, the distribution to Mr. Lord of profits and surplus account. We do not see the materiality. If counsel [156] says in his statement to us that he wants to round out the picture, and get everything before it, that is all right, but we want to know if it shows any different set-up than we contend for. That is the original sixty thousand dollar capital contributed by Mr. Lord and undivided profits carried in the surplus account. If it does, we should certainly like to amend our set-up, because we do not contend for anything different than the distribution of sixty thousand dollars in capital and the balance in surplus and undivided profits, and if there are

*Omitted from printed record on stipulation by counsel.

any figures that change that, that counsel in argument or otherwise after the case closes contends is incorrect, as a matter of computation, we should like to know it now; because our desire is to go to this board practically on an agreed state of facts. We do not believe there is any room for any argument or any disagreement between the Government and ourselves on the facts. As far as the application of those facts to the law is concerned, that is a matter, of course, on which we are going to disagree and on which the Board has to decide, but we do not want this Board to have any disagreement as to the facts, and if counsel's argument will show any different set-up than the evidence of Mr. Camp, we should like to know it.

Mr. KAY: Counsel is going to the very issues when [157] he asks to be informed as to what we intend by the introduction of these particular exhibits. The Board will recall counsel has offered on behalf of the taxpayer excerpts from the company's books, E. J. Lord, Limited, and E. E. Black, Limited, and in offering those excerpts they have taken those piecemeal, and they feel it sets out the picture according to what they think is helpful to them and their contentions. We think we should fill out the picture and bring to this Board all parts of the books of the company. That will give to the Board the entire picture. I might state that carried under assets in these trial balances are the item "Treasury stock, \$273,853." and right on through these trial balances will be found that entry. The Board is familiar with our position, to-wit, that

the transaction involved here was not a transaction in the nature of distribution of dividends by E. J. Lord, Limited, but an out and out sale of stock by E. J. Lord to E. J. Lord, Limited, and, consequently, in support of our contentions, we offer this particular exhibit. I think it is relevant and goes to show the set-up as it actually was.

Mr. PETERS: With that understanding, whatever consolation counsel gets out of the fact that in the interim between December 13, 1929, and February or March, 1931, when the redemption was finally [158] consummated, whatever consolation counsel gets out of that he is entirely welcome to. I might say to the Board on this question of an out-and-out sale of stock the Board must bear in mind we do not contend there was not a sale of stock. Our contention is that every voluntary redemption of stock involves two elements. The first step in the voluntary redemption of stock is the purchase of the stock that is desired to be redeemed, and the second step is the retirement of that stock, either in the possession of a corporation or in the possession of outside parties. When stock comes into a corporation with the idea of retaining it, it is an out and out purchase. When it is bought with the purpose of redeeming it it is an out and out purchase. You cannot have a voluntary redemption without a purchase, whether that purchase be for cash alone or whether it be part cash and part specie or the transfer of assets belonging to a corporation represented by the value of the purchased stock. We have never contended that as far as the first step is concerned in the process of the inten-

tion of the corporation to redeem its stock,—we have never contended that the first step was not a purchase, but we have said the character of that act, its legal effect, was reflected by the intention of the parties. That is the reason for the evidence of Mr. Buchholtz, the evidence of myself, [159] and the evidence of Mr. Black,—to show the intentions. The mere fact that there was a purchase does not mean anything. It is the intention with which it was done. A deed may be a mortgage, a loan may be a conditional sale, a mortgage may be a conditional sale, it all depends on the intention of the parties when the original agreements are entered into. I do not want to go into the merits of this thing at the present time. The Board is going to have sufficient when we argue this out, but I do not want the Board to get any erroneous idea as to the situation as stated by counsel. We have two methods of retirement of stock. One is a voluntary method and the other is involuntary. That voluntary retirement may involve one holder of stock. You cannot proceed to the redemption of that stock unless the corporation acquires it. If it acquires it for the purpose of redemption that is one thing; if it acquires it for the purpose of selling it again, putting it out in the hands of other parties, of course that is a purchase of stock, just as if it would purchase the stock of any corporation, hold it and pass it on for value, but, if the corporation is purchasing it for redemption, it must buy it. It cannot take it away involuntarily. It can say everyone shall produce and hand to the corporation ten or

twenty per cent. of its stock, for which they shall have paid part, plus the [160] undivided profits or surplus, so it is the intention with which they go into it in the first instance. If it is a question of involuntary retirement, the stockholder has no volition in the matters, according to the by-laws. Just as soon as there is a voluntary redemption of stock resulting from an agreement between the corporation and individual stockholder or stockholders it is a question of intention. If there is anything that is incorrect so far as we are concerned in the matter of figures we want to make it correct.

The CHAIRMAN: Objection overruled.

(Document offered in evidence received and marked: "Tax Assessor's Exhibit B.")*

Mr. KAY: We offer next copy of the investment account taken from the books of E. J. Lord, Limited, or E. E. Black, Limited, and likewise a copy of the stock account taken from the same source, and ask that the same be marked.

Mr. PETERS: Subject to our checking, so there be no inaccuracies.

Mr. WRENN: We understand this heading is not taken from the books. We would like to have you lay the foundation before introducing it.

Mr. KAY: Mr. Glass informs me those headings are explanatory notes, but the items are all exact copies of the items appearing in the books. [161]

(Documents offered in evidence received and marked: "Tax Assessor's Exhibit C" and "Tax Assessor's Exhibit D.")

*Omitted from printed record on stipulation by counsel.

TAX ASSESSOR'S EXHIBIT C
E. J. LORD, LIMITED OR E. E. BLACK, LIMITED
BOOKS OF ACCOUNT

Securities Purchased, also Securities Received in Payment of Contracts,
by E. J. Lord, Limited, and Successors.

Date	Name of Security		Par Value	Amount Paid
Sept. 12, 1927	Lihue Plantation Co.—	Trust Notes	\$10,000.00	\$10,000.00
Sept. 12, 1927	Crown Willamette Paper Co.	Bonds	10,000.00	10,200.00
Sept. 12, 1927	Minnesota Power & Light Co.	Bonds	5,000.00	5,075.00
Sept. 27, 1927	Arkansas Power & Light Co.	Bonds	10,000.00	9,750.00
Sept. 27, 1927	Northern States Power Co.	Bonds	5,000.00	5,200.00
Dec. 17, 1927	Columbia Steel Corp.	Bonds	5,000.00	4,987.50
Dec. 17, 1927	Alabama Power Co.	Bonds	10,000.00	10,425.00
Dec. 17, 1927	Los Angeles Gas & Electric Co.	Bonds	5,000.00	5,150.00
Dec. 17, 1927	Sierra & San Francisco Power	Bonds	5,000.00	5,112.50
Feb. 9, 1928	Appalachian Elec. Power Co.	Bonds	10,000.00	10,075.00
Feb. 9, 1928	Texas Power & Light Co.	Bonds	10,000.00	10,100.00
Feb. 9, 1928	Seattle Lighting Co.	Bonds	15,000.00	14,625.00
May 29, 1928	Emporium Capwell Corp.	Bonds	10,000.00	9,750.00
May 29, 1928	East Bay Water Co.	Bonds	5,000.00	5,037.50
Nov. 2, 1929	Lihue Plantation Co.—	Trust Notes	5,000.00	5,000.00
July 8, 1930	Hawn. Bitumals Co. Stock 40% of \$5000.			2,000.00
Sept. 24, 1930	Hawn. Bitumals Co. Stock 20% of \$5000.			1,000.00
Oct. 30, 1930	60 Shares Theo. H. Davies 7% Pfd.			6,030.00
Dec. 31, 1930	Adjustment of Premium & Discount on bonds disposed of.			337.50
				<u>\$129,855.00</u>
Deduct:				
Dec. 11, 1929	Redeemed—Columbia Steel Corp.	Bonds		5,000.00
	Total amount of bonds given to E. J. Lord in payment of his stock			<u>69,000.00</u>
Dec. 31, 1930	Balance in Investment Account			\$55,855.00
	Notes Receivable—Purchased			
Apr. 20, 1929	Honolulu Iron Works			50,000.00
July 9, 1929	Hawaiian Trust Company			50,000.00
	St. Louis Heights Improvement Bonds			<u></u>
	Received in payment of Contract:			
Sept. 30, 1929	St. Louis Heights Improv. Bonds		25,000.00	25,000.00
Oct. 31, 1929	St. Louis Heights Improv. Bonds		16,500.00	16,500.00
Nov. 30, 1929	St. Louis Heights Improv. Bonds		25,500.00	25,500.00
Dec. 31, 1929	St. Louis Heights Improv. Bonds		39,000.00	39,000.00
Dec. 31, 1929	St. Louis Heights Improv. Bonds		12,500.00	12,500.00
Jan. 1, 1930	St. Louis Heights Improv. Bonds		19,500.00	19,500.00
				<u>138,000.00</u>
Deduct:				
Sept. 30, 1929	To Honolulu Iron Works—on account Given to E. J. Lord in payment of his stock			19,000.00
				<u>119,000.00</u>
Feb. 28, 1930	St. Louis Heights Improv. Bonds		40,500.00	40,500.00
Apr. 30, 1930	St. Louis Heights Improv. Bonds		60,500.00	60,500.00
Apr. 30, 1930	St. Louis Heights Improv. Bonds		45,000.00	45,000.00
June 30, 1930	St. Louis Heights Improv. Bonds		62,500.00	62,500.00
July 30, 1930	St. Louis Heights Improv. Bonds		5,551.26	5,551.26
				<u>214,051.26</u>

Date	Name of Security	Par Value	Amount Paid
Deduct:			
Mar. 31, 1930	To Theo. H. Davies & Co.—on account	15,000.00	15,000.00
July 31, 1930	Sold to Liberty Bank	50,000.00	49,000.00
	Discount on above sale		1,000.00
July 31, 1930	Given to E. J. Lord in payment of his stock	23,000.00	23,000.00
Dec. 31, 1930	Given to E. J. Lord in payment of his stock	68,000.00	68,000.00
			<hr/> 156,000.00
Dec. 31, 1930	Balance in St. Louis Heights Bond Account		\$58,051.26

Securities and Cash given to E. J. Lord in Payment of his Stock holdings in
E. J. Lord, Limited, Etc.

Date	Name of Security	Par Value	Amount
Feb. 28, 1930	Lihue Plantation Co. Trust Notes	\$10,000.00	\$10,000.00
Dec. 31, 1930	Arkansas Power & Light Co. Bonds	10,000.00	10,000.00
Dec. 31, 1930	Alabama Power Co. Bonds	10,000.00	10,000.00
Dec. 31, 1930	Texas Power & Light Co. Bonds	10,000.00	10,000.00
Feb. 28, 1930	Seattle Lighting Co. Bonds	15,000.00	15,000.00
Dec. 31, 1930	Emporium Capwell Corp. Bonds	9,000.00	9,000.00
Feb. 28, 1930	Lihue Plantation Co. Trust Notes	5,000.00	5,000.00
			<hr/> 69,000.00
Feb. 28, 1930	Honolulu Iron Works		50,000.00
Feb. 28, 1930	Hawaiian Trust Company		50,000.00
Feb. 28, 1930	St. Louis Heights Improv. Bonds	119,000.00	119,000.00
July 31, 1930	St. Louis Heights Improv. Bonds	23,000.00	23,000.00
July 31, 1930	St. Louis Heights Improv. Bonds	68,000.00	68,000.00
July 31, 1930	St. Louis Heights Improv. Bonds		482.36
	Accrued Interest		
Feb. 13, 1930	Cash		1,000.00
July 17, 1930	Cash		373.00
Dec. 26, 1930	Cash		68,313.98
			<hr/> 449,169.34
Dec. 31, 1930	Amount shown in the Treasury Stock Account		
Entry in 1931—for 40% Federal Taxes		26,904.66	
Feb. 28, 1931	To Treasury Stock Account		
Less:			
May 31, 1931	Adjustment—Stock Account	6,576.16	20,328.50
			<hr/> \$469,497.84
Settlement—Interest not charged to Treasury Stock Account—Dec. 31, 1930		\$ 1,277.86	

Note:

Dates and figures shown on this statement were taken from the Books of Account of the Company.

TAX ASSESSOR'S EXHIBIT D
E. J. LORD, LIMITED, OR E. E. BLACK, LIMITED.
 Schedule Showing Original and Re-issued Certificate—E. J. Lord, Limited, & Successors—Taken from the records of the Company.

No. of Certificate Original Re-issued	Date	Name	No. of Shares	Transferred to:	Date	No.	Certificates Surrendered
No. 1	Sept. 3, 1926	E. J. Lord	800	E. J. Lord & E. E. Black	Nov. 8, 1926	1	800
2	Sept. 3, 1926	E. E. Black	197				
3	Sept. 3, 1926	Geo. Buchholtz	1	E. E. Black	Oct. 1, 1926	3	1
4	Sept. 3, 1926	P. J. Erben	1	E. E. Black	Oct. 1, 1926	4	1
5	Sept. 3, 1926	T. Ikejiri	1	E. E. Black	Oct. 1, 1926	5	1
No. 6	Oct. 1, 1926	E. E. Black	3				
7	Nov. 8, 1926	E. J. Lord	310	Treasury Stock	Feb. 15, 1930	7	310
8	Nov. 8, 1926	E. J. Lord	200	Treasury Stock	Feb. 15, 1930	8	200
9	Nov. 8, 1926	E. J. Lord	90	Treasury Stock	Feb. 15, 1930	9	90
10	Nov. 8, 1926	E. E. Black	200	E. E. Black, etc.	Feb. 15, 1930	10	200
11	Feb. 15, 1930	E. E. Black	196				
12	Feb. 15, 1930	E. J. Lord	1	E. E. Black	Feb. 15, 1930	12	1
13	Feb. 15, 1930	Geo. Buchholtz	1	E. E. Black	Feb. 15, 1930	13	1
14	Feb. 15, 1930	J. P. Erben	1	E. E. Black	Feb. 15, 1930	14	1
15	Feb. 15, 1930	T. Ikejiri	1	E. E. Black	Feb. 15, 1930	15	1
16	Feb. 15, 1930	E. E. Black	4				

[260]

Mr. KAY: We offer letter dated December 19, 1930, rather, copy of letter dated December 19, 1930, addressed to Mr. E. J. Lord, care of Hawaiian Trust Company, Limited, from E. E. Black, Limited, referring to the transaction under subject of inquiry before this Board, a copy is offered as being an exact copy of the letter in the files of E. E. Black, Limited.

Mr. WRENN: Is that letter compared with the original from which it was taken?

Mr. KAY: I will give you a copy and upon subsequent check we shall be glad to correct the same.

Mr. ADAMS: You purport to furnish us a true copy?

Mr. KAY: Yes.

(Document offered in evidence, consisting of three pages, received and marked: "Tax Assessor's Exhibit E.")

TAX ASSESSOR'S EXHIBIT E.

3 Papers.

[Seal]

TERRITORY OF HAWAII
TREASURY DEPARTMENT.
HONOLULU.

December 19, 1930. H. T. K.

Mr. E. J. Lord,
c/o Hawaiian Trust Co., Ltd.,
Honolulu.

Dear Sir:

Enclosed please find in duplicate Auditor's Report, with accompanying Balance Sheet and Statement of Profit and Loss for the period, ending

letter of Mr. L. N. MacComiskey, dated December 17th, 1930, showing Federal and Territorial Taxes computed on the profits of the Contracts in which you have an interest, as in our agreement with you dated December 13th, 1929. We wish to mention here that the Federal Income Tax has been computed at the rate of 12%, as it is practically a certainty that the tax rate will be raised from 11% to 12% for this year's earnings. We will have a document drawn up, stating that in case the tax rate should not be 12% we will reimburse you with the difference, and will hand you the document at the time of settlement.

From the Auditor's Report and Mr. MacComiskey's letter we get the following:

Profits from Contracts: (as specified in Agreement of Dec. 13, 1929)	\$588,039.89
Less:	
Taxes (as computed in Mr. Mac- miskey's letter, Dec. 17, 1930)	95,567.93
Net Profits on above Contracts	<u>\$492,471.96</u>
60% of \$492,471.96, due you	\$295,483.18
Less:	
Paid on account (as per State- ment Dec. 31, 1929)	124,947.06
	<u>170,536.12</u>
Plus:	
Additional for Plant (as agreed)	3,500.00
	<u>\$174,036.12</u>
	<u>[261]</u>

2.

Furthermore, we are liable for 40% of your Federal and Territorial Income Taxes to which you may become liable upon income accrued by reason resulting from the sale of the 600 shares of E. J. Lord to us. This is payable upon assessment, as per agreement of December 13, 1929, and will be paid by us to you, or designated representative at such time as it is due.

We propose to pay you in the following manner, this giving you not more than 60% of the St. Louis Heights Bonds received, and not more than 60% of Industrial Bonds we had in possession in December 1929.

- | | |
|---|-------------|
| (1) St. Louis Heights Improvement Bonds at 5%—136 at \$500. with coupons attached from August 15, 1930. | 68,000.00 |
| (Interest see below) | |
| (2) Industrial Bonds | \$39,000.00 |
| 10 Arkansas Power & Light Co., 5½% \$10,000.00 | |
| with coupons attached from Oct. 1, 1930. | |
| (Interest see below) | |
| 10 Alabama Power Co. 5% | 10,000.00 |
| with coupons from Dec. 1, 1930. | |

10	Texas Power & Light Co., 5%	10,000.00
	with coupons from Nov. 1, 1930.	
9	Emporium Cap- well Corporation, 5½%	9,000.00
	with coupons from Oct. 1930	_____
(3)	Cash	67,036.12

	making a total of one hundred seventy- four thousand thirty-six 12/100 dollars	<u>\$174,036.12</u>

We also propose to pay to you the sum of \$607.50 being interest on above bonds from August 1st, 1930, in lieu of interest coupons computed as follows:

St. Louis Heights Impr. Bonds—	
½ month at 5%	\$141.67
Arkansas Power & Light Co.—	
2 months at 5½%	91.66
Alabama Power Co.—	
4 months at 5%	166.67

Forward—	\$400.00
	[262]
Bro't Forward	\$400.00
Texas Power & Light Co.—	
3 months at 5%	125.00
Emporium Capwell Corp.—	
2 months at 5½%	82.50

	<u>\$607.50</u>

Trusting this will meet with your approval and awaiting a reply what day will be suitable to make the settlement, we remain,

Very truly yours,

E. E. BLACK, LIMITED,

By.....

Treasurer.

[263]

HENRY GLASS

was duly called and sworn as a witness for the Tax Assessor, and testified as follows:

Direct Examination by Harold T. Kay, Esq.

Q. State your name and occupation?

A. Henry Glass.

Q. Your occupation? [162]

A. Income Tax Assessor, Territory of Hawaii.

Q. You are income tax assessor for the Territory of Hawaii?

A. Yes.

Q. For how long have you served in that capacity?

A. Since January 1928.

Q. Was there any income tax return filed by E. J. Lord for the year 1930?

A. Yes.

Q. When was that filed?

A. The return was filed March 2, 1931.

Q. By whom?

A. By the Hawaiian Trust Company, account of E. J. Lord.

(Testimony of Henry Glass.)

Q. Will you state whether that return is in the record here or a copy thereof?

A. There is a copy.

Q. What does that return show?

A. Gross income, \$527,598.20; deductions, \$534,543.78; deficit \$6,945.58.

Q. Mr. WRENN: Is there any point that this is not correct?

Mr. KAY: That is part of the record.

Mr. ADAMS: It came up to us on appeal.

Q. What else does it show?

A. Exemption of \$1400., personal exemption.

Q. How is the sale of stock by E. J. Lord to E. J. Lord, Limited, reflected? [163]

A. Under item 8, dividends from corporations subject to Territorial income tax, an item E. J. Lord, Limited, \$512,838.54. That was supposed to be—

Mr. PETERS: I object to what it was supposed to be.

Q. Is there any other reference to that?

A. Item 8 refers back to Schedule B.

Q. What does Schedule B show?

A. Schedule B shows profit from sale of real estate, stocks, bonds, and so forth. That is the heading of Schedule B and under the items it says "Kind of property, stocks. Date acquired, 1926; date redeemed, 1930; redemption \$60,000."

Q. Anything else shown?

A. Cost price sixty thousand dollars; net profit none.

(Testimony of Henry Glass.)

Q. What is the total of that schedule?

A. Profit from sale of real estate, stocks, bonds and so forth. And there is another memo, redemption sale of 600 shares of E. J. Lord, Limited. It says here in one of the columns, the column is printed: "Selling price" and the words "selling price" seems to have been attempted to be ruled out, and the word "redemption" put on top of it. We have no such word in any Territorial Income Tax law.

Mr. ADAMS: Do those words refer to an item of the schedule?

A. Schedule "B" is used, should be put under item 5. It would naturally go there. Schedule "B" would [164] naturally go under item 5. I don't know why they put it in that way. It does go under the last column of schedule "B." It shows "net profit, none" so of course there would be "none" under column 5, but they show here \$512,838.54.

Q. Was there any taxable income shown by that return?

A. None.

Q. Any deficit?

A. Deficit 6945.59.

Q. The examination of that return, did your office make an examination of the books of E. J. Lord, Limited?

A. To a certain extent.

Q. And as a result of that examination what action was taken by your office?

(Testimony of Henry Glass.)

A. I found there was a sale of stock in our opinion by E. J. Lord, and we decided to assess on the profit that he had derived from the sale of stock.

Q. Was such an assessment made?

A. Yes, sir.

Q. What was the amount of that assessment, handing you copy of proposed change in assessment of income tax return of E. J. Lord? Will you refresh your memory?

A. We sent them as required by law notice of proposed change in assessment on income tax return, dated May 14, 1931.

Mr. PETERS: That was sent by registered mail? [165]

A. By registered mail.

Mr. PETERS: And you have the receipts for it?

A. Yes.

Q. Give the details?

A. Gross income, first return, \$527,598.20; deductions, first return, 534,543.78; exemptions, \$1400. In the next column, as changed, gross income, 430,833.66; deductions 21,705.24; exemptions \$1400.; net taxable income \$407,728.42; tax 19,161.42.

Q. What was done in respect to that assessment by Hawaiian Trust Company or E. J. Lord?

A. Nothing that I know of.

Q. Subsequently did Hawaiian Trust Company file on behalf of E. J. Lord an amended return?

A. Yes.

(Testimony of Henry Glass.)

Q. Referring to the record, will you state whether that amended return is part of the record?

A. Yes.

Mr. WALSH: Yes, what?

Q. Is that return part of the record?

A. It is.

Q. What date was that filed with the income tax bureau?

A. January 18, 1931.

Q. Who delivered it to your office?

A. By Mr. Camp.

Q. What does that return show?

A. Gross income, \$421,329.64; gross deductions, [166] 428,275.22; deficit 6,945.58. You want the details of the income and deductions?

Q. Yes?

A. Income, item 3, 9969.99.

Mr. WRENN: Isn't the return the best evidence?

Mr. KAY: Yes, but it is explanatory.

A. (Continuing) Item 8, dividends from corporations subject to Territorial income tax, Pioneer Mill Company, \$580.; Maui Agricultural, \$1308.; E. J. Lord, Limited, \$406,569.98. (See schedule.) A total of 408,547.98; item 8b, 2901.67; deductions: Interest,—

Q. Passing from deductions to the reverse of the income return, will you state what is shown on Schedule "B" entitled "profit from sale of real estate, stock, bonds, and so forth?"

(Testimony of Henry Glass.)

A. Schedule "B" should be the profit from sale of real estate, stock, bonds, and so forth, but the word "sale" has been obliterated and the word "redemption" put on top of it, and the item "Kind of property"—

Q. Do these same items appear in respect to this return under Schedule "B" as appear in the first return?

A. Yes, only they do not put in item under redemption column. There is no redemption column in our return. They have scored the selling column out. Let me [167] give the items of Schedule "B." "Kind of property, 600 shares of E. J. Lord, Limited. Date acquired; 1926. "Date sold, it should be, but the word "sold" is obliterated and the word "redeemed" put in its place,—"1930; cost price sixty thousand dollars; net profit, none."

Q. Was an assessment made in respect to that amended return by your office?

A. Yes.

Q. Will you state what is the date of that assessment and what the assessment was?

A. June 19, 1931, as returned gross income 527,598.20; deductions, 534,543.78; exemptions, \$1400. As changed: Gross income, 421,329.64; deductions, 21,705.24; exemptions 1400.; net taxable income, 398,224.40; tax, 18,686.22.

Q. To whom was that notice of assessment delivered?

A. To Mr. Carter Galt of the Hawaiian Trust Company.

(Testimony of Henry Glass.)

Q. By whom?

A. By me.

Q. On what date?

A. On June 19th.

Q. And that was the day after you received the amended return, was it?

A. Yes.

Q. Can you state from your own knowledge whether the appeal now pending before this Board was filed prior to or after the filing of the amended return [168] and assessment made by you?

A. I don't recall.

Q. Was it before or after?

A. It was after the assessment was made, because the—

Mr. PETERS: It was after the amended assessment?

A. Yes, the assessment dated June 19th. The Hawaiian Trust Company rang me up. I think it was Mr. Camp, after he had filed the amended return on June 18th, and requested that a notification be given him the next day, if possible, of the assessment we intended to make. I assured him at that time I couldn't possibly verify the existing figures in a day. So I thought it over, however, and the next morning I thought we will cancel the original assessment and we will make an assessment based on this amended return of June 18th and hand it to him, as he said their lawyers wanted to appear immediately, so just to be sure it got

(Testimony of Henry Glass.)

into the proper hands, I got them to make out the notice and took it down myself and delivered it myself to Mr. Carter Galt.

Q. Carter Galt is an officer of the Hawaiian Trust Company?

A. I believe he is.

Q. And the original assessment against the first return was cancelled?

A. That cancelled that.

Q. And the appeal before this Board relates to the part on the amended return? [169]

A. This \$18,000. tax which we assessed.

Q. Your staff has made an examination of the books of E. J. Lord, Limited?

A. We have made a partial examination to satisfy ourselves on this.

Q. As a result of that examination what conclusion did your department reach and did you reach as Assessor in respect to the contention made by the Taxpayer that the payment made by E. J. Lord, Limited, to E. J. Lord for the 600 shares of stock was simply a dividend and was not a payment as and for the purchase of stock?

A. We thought it was a sale of stock, just like any other sale of stock. The question of whether the purchaser gets the money and what he intends to do with the stock after he buys it is not a question for the Government. The purchaser may claim a loss on the sale of the stock or he may make a gain on the sale of his stock. The government does not inquire into the question where the purchaser

(Testimony of Henry Glass.)

of the stock got the money or what he is going to do with the money. The assessment was made against E. J. Lord because he had sold his stock in the corporation. Did you say something about dividends?

Q. Did you find from the books of E. J. Lord, Limited, that a dividend in the amount paid to E. J. Lord had ever been declared?

A. No, there was no dividend declared. [170]

Q. There was not?

A. We examined the minutes about that, and it is impossible that a dividend could be declared to one stockholder, that is against the law, and the books of account December 31st would not support any suggestion of dividend because the books of account to December 31st of E. J. Lord, Limited, and E. E. Black, Limited, showed that the stock was carried in the Treasury stock account. There was no suggestion of a dividend at all even in the books of account of the company.

Q. Did you find appearing in the books of account and other records of the company the expression: "Sale of stock by E. J. Lord and purchase by E. J. Lord, Limited"?

A. They had a supplement account in their books of account of the corporation, E. J. Lord, Limited, and E. E. Black, which spoke of cash and securities being handed to E. J. Lord for the purchase of his stock, 600 shares.

Q. In determining the taxability of gains resulting from the sale of stock did you have occasion

(Testimony of Henry Glass.)

to refer to any of the provisions of our statutes which throw enlightenment upon the matter?

A. Our law is very clear and very specific. It definitely states that income includes gains, profits and income derived from sales of moveable property, [171] less the cost of purchasing and producing the same. These are almost the actual words in the Statute?

Q. That provision occurs in the income tax statute?

A. Yes, I think it is 1390, the Territorial income tax law taxes two separate and distinct gains.

Mr. ADAMS: To save time, here is 1390.

A. Yes, section 1390, I quoted just now. The Territorial Income Tax law.

Mr. WRENN: Just what question are you answering now?

A. The provisions of the law.

Mr. KAY: The provisions of law he had to refer to in arriving at his decision that this was a taxable gain.

The WITNESS: The Territorial income tax law taxes two separate and distinct gains: A gain arising from the operations of a corporation, and the use of its property; and, secondly, any gain there may be from a sale or disposition of its property.

Q. You said a corporation. Does that likewise apply to individuals?

A. Likewise applies to an individual if he is carrying on a business. And the second point applies both to individuals who are not carrying on a

(Testimony of Henry Glass.)

business and to corporations. That second point is popularly called "Capital loss". Our laws are committed to that just the same as the Federal government. It is well understood. Taxpayer's [172] in this community will understand it.

Mr. WRENN: Objected to as a conclusion of the witness.

Mr. KAY: This witness has a right to testify as to the contemporaneous understand of the community.

Mr. WRENN: I urge my objection as a mere conclusion of the witness.

Mr. KAY: I think it is quite common to show contemporaneous construction. The administration of the statute by the tax officials is charged with the duty of administering.

The CHAIRMAN: Objection overruled.

Mr. ADAMS: I think he can testify as to the practice and whether or not he has been collecting from the public in general.

Mr. KAY: I think that is what he is saying.

Mr. PETERS: If it is the understanding in cases of redemption, voluntary redemption of stock. Apparently Mr. Glass makes no distinction between the purchase by the corporation of its outstanding stock for the purposes of reselling and the purchase for purpose of redemption. I think this is all an explanation to the Board as to how we arrived at it. I haven't objected because I thought the Board would like to see how he arrives at his conclusion, get his mental processes. [173]

(Testimony of Henry Glass.)

Mr. ADAMS: If it illustrates his practice, I should think it should be given.

Mr. PETERS: Let it be understood that the practice as to mere sales or purchase by the corporation of its own stock, or in cases of redemption, there might be a distinction in the practice.

Q. What has been the practice in the past followed by your office in respect to the taxation of gains resulting from the sales of stock?

Mr. PETERS: Objected to as immaterial unless it appears they are gains resulting from sale of stock. There are instances where the sale of stock is made to a corporation under agreement of redemption and purpose of redemption by the corporation.

Mr. ADAMS: I think that will all come out in the answer.

A. The practice has been to tax any gains under the appropriate rate under the Territorial income tax law, and also to allow the taxpayer to deduct any sustained loss on disposition of his stockholdings in a corporation.

Q. Is there any provision in the Territorial income tax law or has there been any practice followed by your department recognizing a redemption of stock as such or a liquidating dividend as such?

Mr. WRENN: Objected to as more than duplicitous, and it is incompetent, irrelevant and immaterial unless [174] it shows the department has dealt with the question of liquidating dividend. Let's find out if he has dealt with liquidating dividend.

(Testimony of Henry Glass.)

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(Testimony of Henry Glass.)

Mr. ADAMS: That can all be brought out.

The CHAIRMAN: Objection overruled.

A. There is no such term as "redemption of stock" in our Territorial income tax law, nor in the corporation law, as far as I have seen. Neither is there such a term as "liquidating dividend" either in the Territorial income tax law or in any other law of the Territory of Hawaii. There is a section in our law which deals with retiring or reducing a number of shares by distributing among its stockholders who may be entitled to the distribution any assets of the corporation not in excess of the value of the remaining shares of the corporation which are not so required. I think you will find that in section 3351, revised laws, 1925. The term "liquidating dividend" is a term used in the Federal internal revenue acts. There is no corresponding term in our law; therefore, we do not know what anyone is talking about when they are talking about liquidating dividend, as far as my business is concerned in applying the Territorial income tax law.

Mr. ADAMS: I don't think he has answered your question. You asked him "What has been his practice." [175]

Q. Will you make that a little bit clearer, the matter of practice?

(Question read by the reporter as follows:

"Is there any provision in the Territorial income tax law or has there been any practice followed by your department recognizing a redemption of stock as such or a liquidating dividend as such?")

(Testimony of Henry Glass.)

A. Well, the Territorial income tax bureau cannot apply Territorial income tax law on a question of redemption of stock, because there is no such term in our law.

Q. As a matter of practice has your department taxed all gains resulting from sales of stock in a corporation?

A. Yes, sir; we assess the man that sold, not the man who bought.

Mr. ADAMS: Has there been any practice in regard to the redemption of stock by your department, either redemption of stock or liquidating dividend? Has there been any practice.

A. I cannot answer "yes" or "no." There is no such word as "liquidating dividend" or "redemption." Consequently when you ask me about a liquidating dividend, there is nothing in our law about it.

Mr. ADAMS: We are trying to get the facts.

A. In a similar situation if a stockholder were [176] to offer his holdings, if his ownership of a part of the corporation was bought by the other stockholders, or by whomsoever, it is a sale of stock as far as the Territory is concerned. As far as we know it is a sale of stock. I am talking about the seller. To him it is a sale of stock, and if he gets more than he paid for it, it is a taxable gain under the Territorial income tax law.

Q. And it has been your practice to tax those gains in the past?

A. Yes.

Q. Suppose there has been a redemption of stock, how would you handle it?

A. As far as I know, it is a sale of stock to him.

Q. Can you give us any specific instance?

A. I can't give you any specific instance at the moment. That very seldom happens.

Mr. ADAMS: If there has been any redemption of stock you have handled it, as far as the man whose stock has been redeemed, as a sale of stock on his part?

A. I would naturally do that, handle it that way, if any such thing arises.

Q. You know of no such thing in the past where it has been handled otherwise?

A. No, I don't.

Mr. ADAMS: Has there been any transfer of stock corresponding to such a transaction in the past that has been [177] handled by your department?

A. As I say, I can't give any specific instance. If you ask me today that I will try to look back in the files and probably between us we could look up something like that to find it out, but it is not a thing I can answer yes or no right away. I have two or three instances in my mind, but I would certainly have to look them up to find out what was done first.

Q. It is the contention in this case that the payment made by E. J. Lord, Limited, to E. J. Lord was a dividend of the character that is granted an exemption under the provisions of Section 1391,

(Testimony of Henry Glass.)

Revised Laws, 1925, reading that dividends paid on stock owned on which corporations have paid a two per cent. tax will be exempt. Will you state as a matter of administration of your department whether or what character of dividends therein exempted has been given exemption, and how your department has construed that particular term "dividend" as used in that provision?

A. We naturally refer to the law in that case, and under our law, under the laws of the Territory, "Dividend" is a distribution of profits arising from the business of the corporation. You will find that outlined in Section 3361. That interpretation of the word "dividend" is the accounting interpretation. When an accountant talks about dividends [178] he talks about a distribution of profits which can only be declared by the directors of a corporation and that is the meaning of the word dividend.

Mr. PETERS: That doesn't say so in the Statute. It doesn't say it can only be declared by a dividend in that section.

A. I didn't say so in that section.

Mr. WRENN: That is your idea of what the law is, is it?

Mr. KAY: Just a moment. The witness is on direct examination and you are not required to answer these questions.

Q. The dividend is a matter of practice, the dividend contemplated by section 1391 which is entitled to exemption is the dividend that has been

(Testimony of Henry Glass.)

duly declared by a corporation as a dividend from profits in those cases where the corporation has paid a tax of two per cent.

Mr. WRENN: Objected to as incompetent, irrelevant and immaterial, not shown that the other situation has ever been presented to the Board.

The CHAIRMAN: Objection overruled.

A. Yes.

Q. In the administration of your department have you ever had occasion to grant exemption or has an exemption been granted in respect to the dividend that was only declared to one stockholder and not declared to all stockholders pro rata? [179]

A. Never that I knew of.

Q. Can you state whether "dividend" as construed by your department, constitutes or consists of a dividend from profits duly declared by a corporation to its stockholders pro rata?

A. Yes, sir.

Q. That is what you understand "dividend" to mean as used in Section 1390?

A. Yes, sir.

Q. In respect to that exemption as granted in Section 1391 can you state whether or not there was any significant fact appearing in the transaction between E. J. Lord and E. J. Lord, Limited, which clearly takes it from that exemption, the particular transaction. I am referring particularly to the surrender of the stock by E. J. Lord. How can that be resold with the provisions of 1391.

(Testimony of Henry Glass.)

Mr. PETERS: Objected to as unintelligible, argumentative, duplicitous, and asking for a conclusion of the witness as to an interpretation of the section of the law.

Mr. KAY: I will reframe it.

Q. Referring to section 1391 it is "provided further that in assessing the income of any person or corporation there shall not be included the amount received from any corporation as dividends upon the stock of such corporation if the tax of two per centum has been assessed." In the case before the Board and [180] in the facts thus far adduced in your opinion can it possibly be said that this payment could have been a dividend upon the stock owned of E. J. Lord, Limited?

Mr. WRENN: Objected to as calling for a conclusion of the witness on a question of law.

Mr. ADAMS: Not a question of law, but in the practice of the Assessor's department.

Mr. WRENN: There appears to be no practice. How could he go into that?

Mr. ADAMS: Will you form your question again, to make it the practice of his department.

Q. In the administration of your department and the construction followed by your department in the last proviso in Section 1391, will you state whether it has been the practice to consider payments from corporations as dividends when issued to a stockholder by virtue of ownership of stock?

A. Yes, sir; that always would be considered dividends, and that was the practice of the office

(Testimony of Henry Glass.)

to allow dividends which have been paid by corporations which had been assessed under the Territorial income tax law to be exempt from taxation themselves.

Q. Is a surrender of stock in consideration of the payment, could that possibly as a matter of administration be construed as a dividend?

Mr. WRENN: Objected to as calling for a conclusion of the witness and a conclusion of law. [181]

Mr. ADAMS: I think that is all right. It is a matter of administration. His department administers the law.

The CHAIRMAN: Objection overruled.

A. Of course it is not a dividend because when the corporation pays a dividend the stockholder does not relinquish the stock. We cannot consider the question at all. There is a difference between the stockholder getting his dividend and the stockholder disposing of his holdings; they are two entirely different things.

Q. Have you had occasion to refer to that provision of law providing that shares of stock of a corporation shall be considered as personal property?

A. Yes, we have all those things in our mind. The law distinctly states that shares in a corporation are personal property.

(Adjourned subject to call.) [182]

[Title of Court and Cause.]

The above entitled matter came duly on for further hearing before the aforesaid Board on Monday, December 28, 1931, at 2 o'clock p. m., all members of the Board and all parties to the hearing being present, and the following further proceedings were had and testimony taken:

HENRY GLASS,

a witness for the Tax Assessor, resumed the stand and testified as follows:

Cross Examination by Emil C. Peters, Esq.

Q. Just by way of resume, is there any case that you can remember in the Tax Office in which there has been a voluntary reduction of stock?

A. Why do you mean by "a voluntary reduction of stock?"

Q. A redemption of stock as between the corporation and the stockholder, voluntarily entered into between each of them. Do I make myself plain?

A. Yes, but you didn't say what you meant by "voluntary." On the part of the stockholder? [183]

Q. Perhaps I can explain it this way. We are both agreed that the directors are the managers of the corporation?

A. The directors are the directors of the corporation.

Q. The directors are the managers of the corporation?

A. The statute says directors or managers. I assume that is what is meant.

(Testimony of Henry Glass.)

Q. And there is the superior control of the stockholders?

A. Yes, they own the corporation.

Q. There is a superior control of the stockholders?

A. Control in what way?

Q. Of the business of the corporation?

A. The stockholders own the corporation.

Q. Well, they control the business of the corporation? They are superior to the directors, are they not?

A. That is a question of law. I would like to have you decide that for yourself.

Q. I don't want to quarrel with you. You are asking me for a definition and I am trying to give it to you. You do know,—don't you know, that sometimes in the directors and sometimes in the stockholders is reposed the power of reducing the number of shares of capital stock?

A. I think, according to our law, I think it is [184] the stockholders that have the power to reduce the capital. Might we have the revised laws of 1925?

Q. Don't let's bother about that.

A. I would like to have it when I am answering questions along that line.

Mr. KAY: I think the witness has the right to refer to it if he wants to. (Handing copy of the revised laws to the witness.)

The WITNESS: (Witness refers to copy of revised laws) You said reduction of capital? It gives it in section 3351.

(Testimony of Henry Glass.)

Q. You wanted to refresh your recollection. The proposition is that under that Statute a certain percentage of the stockholders regularly assembled can reduce the capital stock, can they not?

A. That is what the section says.

Q. And whether you are a dissenter or not, if the required number of stockholders so vote you have to give up your proportionate holdings in the corporation, would you not, in order to arrive at that reduction?

A. That is a question of law that can all be threshed out in there.

Q. Do you know that?

A. I will give no answer to that.

Q. You are asking me for a definition. I am trying to help you give that definition. Won't you please [185] approach this subject with me in a spirit of friendliness instead of antagonism?

A. Certainly. There is no antagonism.

Q. May it not be so that although a member of a corporation may not be willing to give up his holdings in a corporation, that unwilling member may be forced to by the stockholders in a meeting,—be forced to give up a certain proportion of his stock?

Mr. KAY: Objected to as not proper cross-examination. The witness did not go into the matter of the reduction of stock.

Mr. PETERS: I think we can progress a little more rapidly if we have a little more cooperation from the witness. My position here is a very simple

(Testimony of Henry Glass.)

one. We have a provision for the reduction of the capital stock of a corporation, and that reduction may be accomplished, as you know, by the necessity of the stockholders giving up a certain proportion of their shares; whereas they might hold 100 shares, but, after a 50 per cent. reduction, they would hold 50 shares, and 50 shares would be redeemed. So if we had a 50% reduction and we were stockholders and not be willing to do that, and might vote against it, but by virtue of the fact that the stockholders in regular meeting assembled voted for it, we would have to give up our proportion. That is known as an involuntary method of capital [186] reduction. Now we have certain voluntary methods. The corporation comes to me, like it came to E. J. Lord in this case, and says "We would like to reduce our stock by the holdings which you have at the present time, and that stockholder is not coerced by any provision of the Statute making him give up half of the stock or all of the stock; he voluntarily agrees and assists the corporation in reducing its stock by selling it his stock. And the corporation having acquired it for the purpose of redemption retires it and applies to the Treasurer of the Territory for a reduction of the capital stock. What I want to know is this,—does the witness remember any voluntary reduction of stock as having occurred in the tax office. He comes back with the proposition "What do you mean by 'voluntary,' " and immediately I attempt to define what I mean by "voluntary" and the battle is on.

(Testimony of Henry Glass.)

Mr. KAY: May it please the Board, what Judge Peters has said is a matter of law. If Judge Peters wants to frame his question in the light of argument, what he means by "voluntary reduction" and asks—

Mr. PETERS: Oh, I will withdraw the question.

Q. Do you know of any similar instance in the tax office where the facts are parallel with the instant case, the redemption of Mr. Lord's stock?

A. We have had cases of large losses deducted from income on Territorial income tax returns on liquidation [187] of a company. Would that be something like what you mean?

Q. Are you asking me a question, or are you answering my question?

A. I am answering your question.

Q. Please tell me the names of any companies involving facts similar to the instant case that you have had in that tax office?

A. I don't know anybody that sold 600 shares of E. J. Lord, Limited. I don't know anybody that sold 600 shares of any other corporation, but I do know where a company was liquidated and all of its stock cancelled and the company dissolved and large losses taken off their income tax returns by the stockholders, that may be an analogous case in your mind.

Q. Do you know of any instance in the tax office where the question of taxes has been involved

(Testimony of Henry Glass.)

where an individual has sold his stock in a corporation to the corporation and the corporation has redeemed that stock so purchased?

A. I haven't any in mind just now.

Q. Isn't it a fact that this is the first instance of this kind in your experience in connection with the tax office they have had occasion to meet that?

A. I don't know of any now. I don't remember. I have none in mind now.

Q. All these undivided profits that have been referred to paid taxes, did they not? [188]

A. Which undivided profits do you refer to?

Q. The only ones we have spoken of,—the profits which were paid to Mr. Lord?

A. There were no undivided profits, so far as I know, paid to Mr. Lord.

Q. Haven't we been talking right straight along that the payment to Mr. Lord was composed of sixty thousand dollars of capital originally invested, and the rest was surplus or undivided profits?

A. What was given to Mr. Lord was cash and its equivalent, and you will find on the balance sheet of E. J. Lord, Limited, that that cash and equivalent of cash is carried as the capital of the company, the cash and its working capital and the investments as its temporary investments.

Q. Do you understand that all this time we have been talking about the surplus account and the profits that have gone to that surplus account you haven't considered that as a surplus account?

(Testimony of Henry Glass.)

A. If you will point out the surplus account that you are talking about, I will see whether we considered that a surplus account or not. Are you referring to the surplus account on the books of E. J. Lord, Limited, and E. E. Black, Limited?

Q. What else have we been talking about?

A. Never mind what else we have been talking about. It want to be specific. If that is what you are talking about, there was a surplus on the books of [189] E. J. Lord, Limited, and E. E. Black, Limited.

Q. That surplus had been returned, portions of it had been returned each year and taxes paid on it?

A. I would need to refer to the tax returns to see what taxes had been returned.

Q. They are all in evidence.

A. I assume they are. The amounts shown there I presume were all profits from the activities of the business.

Q. Just answer my question, whether or not this surplus that existed in E. J. Lord, Limited, and E. E. Black, as of the 1st of January 1927, 1928, 1929 and 1930, that the corporation then in existence had paid Territorial income taxes upon?

A. I presume they did.

Q. Can't you say "yes" or "no"?

A. I presume they did.

Q. Can't you say "yes" or "no"?

A. No. You have to examine the books to see that. There may have been exemptions. There may

(Testimony of Henry Glass.)

be items in that surplus that are not taxable under our law.

Q. All the items contained in that surplus that were taxable under the law, income taxes had been paid on it, hadn't they?

A. I presume they were.

Q. If that surplus had been distributed to all the stockholders of E. J. Lord, Limited, and E. E. Black, Limited— [190]

Mr. ADAMS: Why bring in the name of E. E. Black?

The meeting of the stockholders was held on Feby.

~~February~~ 15, 1930, when they voted to disincorporate the company of E. J. Lord, Limited.

Q. This surplus that existed on the 1st of January of 1927, 1928, 1929 and 1930, had it been distributed to all the stockholders of the company at that time, would have been exempt, as far as returned by the individual for income tax purposes, would it not?

A. All dividends payable by Hawaiian corporations that pay 5% taxes on the earnings are exempt under our law?

Q. And if they had been declared as dividends in the previous year or succeeding year a reduction could have been claimed by by the stockholders in the amount they received?

A. I have already stated that dividends to stockholders paid by corporations up to 5% on the net earnings are exempt from taxation on the stockholders return.

(Testimony of Henry Glass.)

Q. So on the 1st day of January, 1930, 1930, this entire surplus could have been distributed to the stockholders then existing and they would have been exempt from any Territorial income tax upon it?

A. I have already answered that question three times.

Q. You have answered it in the affirmative?

A. I have answered that dividends paid to stockholders that have paid the 5% on net earnings are [191] exempt under the Territorial tax laws.

Q. So, if the surplus had been paid as dividends to Mr. Black and the other stockholders, this question would never have arisen? In other words, if Mr. Lord had been paid his sixty thousand dollars and his dividends, this question would never have arisen, would it?

A. They would have been paid the dividend and Mr. Lord would still have held his stock.

Q. If he had been paid sixty thousand dollars for his stock, after all the surplus had been divided, his stock would only be worth sixty thousand dollars?

A. You are going into a lot of suppositions. I don't know what would have happened. I am concerned with facts.

Q. All right, if he had been paid all his share of the profits simply as all other stockholders, and then they had bought his stock for sixty thousand dollars and redeemed it, this question would never have arisen, would it?

A. Would they have had anything to buy stock with after they had paid all that dividend?

(Testimony of Henry Glass.)

Q. Would they not?

A. I don't know.

Q. Suppose they had sixty thousand dollars to pay after they had distributed all of the surplus to all stockholders, and they had bought Mr. Lord's [192] for sixty thousand dollars, and redeemed it, this question never would have arisen, would it?

A. I don't know what would have arisen under supposititious circumstances like that.

Q. Don't you want to answer that question?

A. I have no answer to give to that question except what I am saying.

Q. Take the further supposition that if all the surplus had been distributed in dividends and Mr. Lord's stock had been redeemed for sixty thousand dollars, and the capital stock of the company had been reduced to the value of Mr. Black's stock, and the other three stockholders, this question would not have occurred either, would it?

A. You are making a statement. I don't care to go into that. I have never had that point before,—that point doesn't come up at all on this case.

Q. Take it as a hypothesis?

A. I don't care to.

Mr. PETERS: I would ask that the Board instruct the witness to answer the question. Here is a very simple proposition, so you will understand what I am driving at: According to the evidence 60% of this surplus is turned over to Mr. Lord, plus his original contribution to capital. As far as that

(Testimony of Henry Glass.)

corporation is concerned, they could have distributed the entire surplus existing at that time, could have bought Mr. Lord's stock for sixty thousand [193] dollars. Mr. Black could have turned back his dividend into the corporation and then have gone before the Treasurer's office and reduced the capital of that corporation to the value of Mr. Black's contribution to the 40% of the surplus that he returned.

Mr. WALSH: What is the point of trying to make the witness say that? It seems to me that is an argument before the Board.

Mr. PETERS: As I understood at the last session he was talking about departmental practice, and I am going into departmental practice. I am asking what would have occurred under that hypothetical case down there. I want the Board to understand that if there had been any attempt to evade the payment of taxes, they could have legally have done and accomplished what they did here by distribution of dividends among all those stockholders. Mr. Black could have put his dividend back into the corporation and there would have been no tax assessment under the law, and this question would not have arisen. In other words, it is the tax office which is quibbling here and trying to create a liability which under the circumstances should not exist and never has existed.

Mr. ADAMS: But that is not what has transpired.

Mr. PETERS: We are presenting a hypothetical case, [194] which if we had wanted to go into a lot of red-tape we could have done. Counsel will argue

(Testimony of Henry Glass.)

that dividends must be distributed among all the stockholders. I am trying to show the Board that a dividend by whatever name is a dividend, nevertheless, and to show the Board what we did was not to evade taxes. We did exactly what we could have done by a longer method. We could have declared a dividend of that entire surplus. Instead of that they take a short-cut and they give Mr. Lord his original contribution of capital, and his share of the surplus in the nature of a dividend, and instead of Black taking the dividend that Mr. Lord took and putting it back in the corporation, he takes a short cut and the Territory steps in and says, "You did it that way; the dividend must be to all the stockholders. You can't call that a dividend. A dividend is distributable to all the stockholders according to their holdings" and we are showing by a hypothesis, trying to demonstrate to this Board had we taken the long way around, the red-tape proposition, there would have been no taxation question here at all.

Mr. ADAMS: It seems to me that is a question of argument before the Board. The Tax Assessor's office is bound by the law as it exists.

Mr. PETERS: That's quite true. I thought as Mr. Glass had so learnedly expounded the law and the [195] practice of the Tax Office, I thought that the Board would like to hear what he had to say about this. You would think according to the witness' statement at the last hearing there was a voluntary surrender of stock every day, and yet we haven't an instance of such a thing.

(Testimony of Henry Glass.)

Mr. ADAMS: Why not let it go at that?

Mr. PETERS: All right. It is all right with me. if the Board doesn't want to hear it. That's all I wanted to ask.

Cross Examination by Heaton L. Wrenn, Esq.

Q. As I understand it was in 1928 you first went into the income tax department?

A. That's right.

Q. And you don't intend to qualify here as a lawyer, an expert on corporation law?

A. Oh, no.

Q. You stated in your testimony the other day that it was on March 2, 1931, that the Hawaiian Trust Company, Limited, filed Mr. Lord's income tax return. That was done under a general extension given to the Hawaiian Trust Company?

A. The Hawaiian Trust Company and all its clients.

Q. Prior to the time you became the income tax assessor, what tax experience did you have, Mr. Glass?

A. No particular tax experience. I had made out [196] tax returns at various times, but I have no particular tax experience, no close association with the laws. I had made out Federal taxes.

Q. You made out tax returns occasionally?

A. Yes.

Q. But that was as close as you had ever come to having any experience with tax work?

A. Yes.

(Testimony of Henry Glass.)

Redirect Examination by Harold T. Kay, Esq.

Q. Prior to your appointment as Territorial income tax assessor will you state how many years you had had experience in accounting and keeping of corporation records, books and so forth?

A. Twenty-five years prior to that.

Q. Will you state how many years of the 25 were spent here in the Territory of Hawaii?

A. All of them barring a couple of years in the war service.

Q. Under cross-examination by Judge Peters you refer to dissolutions of corporations where losses were allowed on income tax returns?

A. Yes.

Q. Have you any particular dissolution or dissolutions in mind at this time?

A. We had a very recent one. That was Davies & Company and the Pearl City Fruit Company. Davies & Company were stockholders of the Pearl City Fruit [197] when the assets were liquidated, and Davies & Company as stockholders felt their stock was a loss amounting to about three-quarters of a million dollars, and they deducted from the Territorial income tax returns.

Q. Will you state whether or not Davies & Company were the majority stockholders in the Pearl City Fruit Company?

A. Yes.

Q. As a matter of fact, it owned practically all of the stock in the Pearl City Fruit Company?

(Testimony of Henry Glass.)

A. Yes. There have been a number of other instances of deductions in our Territorial income tax returns by stockholders who have lost money by companies going into liquidation.

HAROLD C. HILL

was duly called and sworn in rebuttal for the Tax Assessor, and testified as follows:

Direct Examination by Harold T. Kay, Esq.

Q. State your name and occupation?

A. Harold C. Hill, tax assessor, First Division.

Q. Territory of Hawaii?

A. Territory of Hawaii?

Q. How long have you held that position?

A. Within a few days of two years.

Q. Appointment as of what date?

A. January 1, 1930. [198]

Q. Prior to that time what was your occupation?

A. For a year and a half collector of internal revenue for the District of Hawaii.

Q. And during that period you were in charge of the administration of the Federal income tax law in the Territory of Hawaii?

A. Yes, sir.

Q. And prior to your appointment as internal revenue collector here in the Territory what position or positions did you hold?

(Testimony of Harold C. Hill.)

A. Approximately three years immediately prior to that time I was income tax assessor for the Territory of Hawaii, and for five years prior to that time I was chief of the division of the income tax collector's office in Honolulu.

Q. You have sat thus far through the hearings in this case?

A. I think I have been present at every session.

Q. You have heard the contention and testimony of the taxpayer's representatives?

A. Yes.

Q. Will you state whether in your opinion the deduction claimed by the taxpayer in this case is a proper deduction under the Territorial income tax law, based upon your experience in administering that law as Territorial income tax assessor?

Mr. PETERS: Objected to as calling for a conclusion of the witness and usurping the functions of this [199] Board.

Mr. KAY: I think it is proper, as the witness has been qualified to express an opinion.

The CHAIRMAN: Objection sustained.

Mr. KAY: May I have an objection to the ruling of the Board sustaining the objection?

Q. In your experience as Territorial income tax assessor will you state whether you recall any deductions such as that claimed by the taxpayer in this case were ever allowed in respect to any Territorial income tax return made by any taxpayer?

(Testimony of Harold C. Hill.)

Mr. PETERS: I object to the question unless it first appears there was a similar case in which the question was raised.

The CHAIRMAN: Objection overruled.

A. I don't recall any such reduction having been made.

Mr. PETERS: Made or claimed or both?

Mr. KAY: I submit if Judge Peters has any questions to ask they may be put on cross-examination.

Q. In your administration as Territorial income tax assessor do you recall whether gains from the sale of stock in corporations were taxed?

A. Yes, they were.

Q. In the Federal income tax law there is a term known as "liquidating dividends" is there not?

Mr. WRENN: Objected to as incompetent, irrelevant and immaterial.

Mr. KAY: That is purely preliminary to show that the [200] Territorial income tax law and Federal income tax law are not similar, particularly as to the term of "liquidating dividends."

Mr. ADAMS: Why don't you ask him a direct question, whether there is any term in the Territorial law similar to the term in the Federal law of "liquidating dividends"?

The CHAIRMAN: Objection overruled.

A. Yes, either in the law itself or in the regulations promulgated by the Commissioner, which have the effect of law.

(Testimony of Harold C. Hill.)

Q. Do you know any similar term in the Territorial income tax law?

A. No I do not.

Q. Will you state whether in your opinion, based upon your administrative experience, both in the Territorial and Federal service, the term "dividend" as used in Section 1391 contemplates or includes the term "liquidating dividend" as that term is generally understood?

Mr. PETERS: Objected to as calling for the conclusion of the witness on a question of law, and usurping the functions of this Board and assuming the fact that there is any understanding in the witness's department as to the meaning of the word "dividend," and an attempt to usurp the functions of this Board, to tell the Board what the meaning of the word [201] "dividend" is.

Mr. KAY: For some reason counsel objects to the Board obtaining the opinions of witnesses as to the administration of the income tax law and in respect to the very matters presented to the Board. We submit the question is entirely proper. If the Board does not care to entertain such evidence, we will defer to the Board's ruling.

Mr. ADAMS: We are not interested in Mr. Hill's opinion. We are interested in the practice of the income tax department of the Territorial tax administration. We assume, and it is proper we should assume so, because the tax administrative officials are presumed to be expert in their line,—

(Testimony of Harold C. Hill.)

we assume they would administrate it according to their interpretation of the law, and they hope to have it sustained in the Courts. His experience, however, in the Federal administration, would have no bearing on his interpreting the Territorial laws. Let's confine ourselves to the practice of the Territorial income tax department.

Mr. KAY: I take it the question will be allowed by deleting the part referring to the Federal service.

(Argument.)

Mr. PETERS: It seems to me counsel confuses his law. We call upon men to testify as to their opinion,—men learned in medicine as to the cause of death, men who by study or observation are skilled in the [202] sciences to give their opinion as to the laws of sciences, and we call men called realtors to give their opinion as to the value of land. Whatever the opinion is, it is finally given by the Court. Suppose that the Court is bothered by the question of Statutory interpretation, would it not be a strange thing to have every attorney in town come and give his opinion as to the Statute. Naturally and properly the Judge would say "Never mind what your opinion is. If you want to argue as to the interpretation of a statute, get appointed as *amicus curiae* or be employed by one of the parties." This Board has first to decide what is the meaning of this word "dividend," and, secondly, whether this distribution was a dividend within

that meaning. Nobody can decide for the Board what is the meaning of that word "dividend" as contained in Section 1391. I am agreed with the Board if there have been any cases of this kind down there and a practice has been followed in disposing of those cases, I think the Board should know, but, if there have been no cases, this witness is not competent to decide.

Mr. ADAMS: Why not ask the witness if in his administration of the Territorial income tax law his department has ever interpreted the word "dividend" as contained in Section 1391 to include what is known in the Federal income tax law as "liquidating dividends"? [203]

Mr. KAY: That is a question of administration. I am now asking a question as to his opinion. I submit he is qualified to express an opinion. However, to meet counsel's objection, perhaps I can reframe this question in such a way that there will be no objection.

Q. If there had ever arisen such a case as is now being presented before this Board, involving a contention that the payment made to Mr. Lord by E. J. Lord, Limited as and for the sale of his stock constituted a liquidating dividend, and, as such, was entitled to be deducted as a dividend under the provisions of Section 1391, would you, as Territorial income tax assessor, have allowed such a deduction?

Mr. PETERS: Objected to as calling for a hypothesis. That is immaterial. That is what this Board is called upon to do. If this question is

(Testimony of Harold C. Hill.)

allowable, why not ask the question "If you, instead of Mr. Glass, had had the duty to determine this matter, what would you have done?"

(Argument.)

Mr. PETERS: My objection is it is not a subject matter of opinion, not a subject matter of expert evidence.

Mr. ADAMS: After all Mr. Hill has been head of the income tax department of the Tax Assessor's office.

The CHAIRMAN: Objection overruled.

Q. (Question read by the reporter.)

A. No, I would not. [204]

Q. You consider the disallowance of the deduction claimed is proper?

Mr. WRENN: Objected to as calling for a conclusion of the witness.

The CHAIRMAN: Objection overruled.

A. Yes, I do.

Q. And that the assessment as made by Mr. Glass is a proper assessment?

A. I believe it to be proper, yes.

Cross-Examination by E. C. Peters, Esq.

Q. Do you know of any case that has occurred in the tax office during your incumbency in which there has been a voluntary reduction of stock of a stockholder of a corporation?

A. I know of a redemption. I don't know whether it is paralled with this case or not. What

(Testimony of Harold C. Hill.)

I have in mind is the Mineral Products Company when they called in their stock and formed the Magnesia Products Company.

Q. That is what I would call an involuntary redemption. Have you finished your answer?

A. I think so.

Q. In the case of the instance which you refer to every stockholder gave up a certain number of shares, or was the par value of the stock reduced?

A. I am speaking from memory on something that happened about 1925 or 1926. As I recall it, I [205] think the stock of the original company, the Mineral Products, was called in and a reduced number of shares in the new company were issued in their stead to those who chose to go on with the company.

Q. In other words, they paid for the redemption of the stock of the Mineral Products with the stock of the newly organized company?

A. You mean the company paid?

Q. You spoke about Mineral Products. I didn't get the name of the second company?

A. Magnesia Products.

Q. The Mineral Products by action of their stockholders reduced their capital stock by retiring a portion of it?

A. Yes.

Q. And then after the reduction or after the amount that still remained did the Magnesia Prod-

(Testimony of Harold C. Hill.)

ucts issue stock to the stockholders of the Mineral Products?

A. Yes, as I recall it, they did.

Q. For the original stock or the redeemed stock. Say, for the sake of argument, I had ten shares of Mineral Products and I was to give up five for the five of Magnesia Products, did I get stock in Magnesia or keep my stock in the Mineral Products and take stock for the five I gave up?

A. I think the Mineral Products went out of the picture. [206]

Q. So, as a matter of fact, it was a complete dissolution and a payment of the stockholders in the old corporation by stock in the new corporation?

A. Yes.

Q. There was no profit involved in that, was there?

A. No, there were plenty of losses.

Q. Let's go back to your statement that according to the income tax statute you would treat this as sales of stock. Gains made by sales of stock were taxed under the income tax law?

A. Yes.

Q. And where a corporation with the intention of redeeming its stock goes out and buys that stock and retires it, would that corporation pay any income tax as a result of that transaction, no matter for what price; can you conceive of the corporation paying any income tax under any state of facts? I would like you to make your own book.

(Testimony of Harold C. Hill.)

Make it any conceivable state of facts by which you can figure up that the acquisition of its own stock by the corporation and its retirement results in a profit to the corporation upon which it would pay any taxes under the Territorial income tax law?

A. I can't draw any situation as that to mind now. I know the Federal government directly states that a corporation cannot either profit or lose by [207] dealing in its own stock, but the Territorial law is entirely silent on that question.

Q. Can you make up any arithmetical problem by which you can compute a profit resulting to a corporation by going out and acquiring its own stock and redeeming it?

A. No, I can't say where there could be any profit.

Q. As a matter of fact, it is not on the cards and it cannot occur. I want to ask you this question: There would have been no objection so far as Mr. Lord and Mr. Black were concerned to claim those as deductions on the ground that the company had already paid the tax, would there?

A. (No answer.)

Q. There are two men that own a corporation and they have three dummy stockholders in order to have a sufficient number of directors under their by-laws. Those two men go to work and figure out that over and above their capital contribution they have a surplus of one hundred thousand dollars

(Testimony of Harold C. Hill.)

profits made in the business, and the corporation has paid from time to time, as this one hundred thousand dollars has accumulated the Territorial income tax on it. Now these gentlemen get together and they have a director's meeting to have distributed that hundred thousand dollars among themselves in the proportion they are entitled to, in proportion [208] to their stock holdings. They would claim their dividends as a deduction, as far as their individual income tax returns are concerned, on the ground that the corporation had already paid the taxes under the statute?

Mr. KAY: Objected to.

Mr. PETERS: I will withdraw the question.

Q. As a matter of departmental practice, has it not been the fact that dividends declared under those circumstances on which the tax has already been paid were claimed as deductions and allowed?

A. You say under those circumstances. If you mean the declaration of a dividend out of surplus, yes.

Q. Let me pursue the situation just a little further. And these two gentlemen agree among themselves that only one shall get a dividend, because the other wants his share of the surplus to remain in the business. He says you take your profits out and I will leave mine in. What is the difference between the hypotheses?

A. That is where I begin to differ with you. I don't think it is a dividend when it only goes to one man.

(Testimony of Harold C. Hill.)

Q. I see what is bothering you. Take a third hypothesis and say that instead of the remaining stockholder leaving his surplus in there he says to the other stockholder, "we will both take it out." "Well," says the first stockholder, "What are you [209] going to do? Are you going on your original contribution of capital?" "Oh, no," he says, "I will take this and claim it as a redemption and put it back into the company as representing my original contribution."

A. You are setting up a situation that did not occur.

Q. Quite right, but the situation as far as Lord and Black are concerned, they could have done it, couldn't they? Couldn't Mr. Lord and Mr. Black have got together and regularly declared a dividend of the entire surplus and both claim a deduction under the income tax law, and E. E. Black, Limited, have gone to the Treasurer's office and reduced it to his original contribution,—in this particular instance forty thousand dollars, and go to work and issue some more stock for the dividend he had received, and then increase it again before the Treasurer's office? If he had done that there would have been no taxes so far as Mr. Lord and Mr. Black were concerned, under those circumstances?

Mr. KAY: Objected to, as the Board is not concerned with what might have been done. We would require the taxpayer to advance the reasons why

(Testimony of Harold C. Hill.)

this procedure was not followed. If it had been followed, a much higher tax might have been paid. There may have been factors affecting such a procedure which would [210] not justify the procedure outlined by Judge Peters. Hence, for Judge Peters to put a question of what might have been done is purely hypothetical and not based on the evidence and facts in the case.

Mr. PETERS: Hasn't Mr. Kay asked the witness what this witness would have done if the case had come before him? All I am asking him is what the actual substance of the whole thing is?

Mr. ADAMS: I assume you are asking him what he would have done if that particular thing had come up.

The CHAIRMAN: Objection overruled.

Q. (Question read by the reporter.)

Mr. KAY: Objected to as duplicitous.

Mr. PETERS: Do you understand the question?

A. I understand what you are driving at all right.

Q. Let me put it this way. Would there be any tax liability as far as Mr. Lord is concerned under the following circumstances: The surplus of E. J. Lord, Limited is regularly distributed as a dividend to stockholders. E. J. Lord, Limited, or E. E. Black, Limited, its successor in name, goes to the Treasurer's office and reduces its capital stock to the amount of remaining capital; subsequently E. E. Black takes the amount he has received by way of

(Testimony of Harold C. Hill.)

this dividend and gain, contributing this to the capital stock, and likewise goes to the Treasurer's office and asks for an increase to meet the increased capital stock. Would there be [211] any income tax liability under the Territorial law so far as Mr. Lord is concerned?

Mr. KAY: Same objection, as it does not state the facts.

The CHAIRMAN: Objection overruled.

A. The first step in your case apparently being that the stockholders of E. J. Lord, Limited, should declare a dividend to all the stockholders?

Q. Yes, including E. J. Lord?

A. Stopping right there, that couldn't be, and I don't see how it could have been taxed under the Territorial law.

Q. And the subsequent acts do not effect the situation whatever?

A. I don't see how they could.

Q. What is the difference between that and the instant case?

A. In the instant case, the ultimate result perhaps is the same, but it is done in an entirely different manner, in that the corporation buys out one of the shareholders and pays that shareholder a price for its stock, a price far in excess of his original contribution, thereby netting him a profit.

Q. So as I understand it, due to the fact that Black did not participate in any dividend, that is the line of demarcation, so it converts the transac-

(Testimony of Harold C. Hill.)

tion entirely, according to your theory, into a sale by the original stockholder to the corporation from which [212] he has derived his profit?

A. Yes.

Q. And it is on the theory of that profit that you impose a tax?

A. That I would have imposed a tax.

Q. Will you tell the Board what kind of a dividend comes within the meaning of Section 1391,—that is the proviso?

A. Any publicly declared dividend,—or, to get away from the dividend, division of a share of the profits of the company which is taxable upon its income within the Territorial laws.

Q. And as a matter of fact, wasn't that just this, a division as between these two stockholders of the profits of that business and a distribution of the share of one to the one?

A. No, I don't think so.

Q. Is the trouble in your mind simply that Black did not get his too? If Black had got his too, it would have been a dividend?

A. I believe so.

Q. If Black had got his 40% and Lord his 60% it would have been a dividend?

Mr. KAY: You have a different situation. You have the situation of control creeping in there. You have a situation where one stockholder passes out of the picture.

(Testimony of Harold C. Hill.)

Mr. PETERS: What has that to do with the definition of the word "dividend"? [213]

Mr. KAY: It has a great deal to do as used in this provision of Section 1391. Dividend contemplates a distribution of earnings on stock that is returning.

Mr. PETERS: It would have been all right on the eve of the first of the year the dividend had been declared to Lord of 60% and on the second they had paid him the \$60,000., is that the idea?

Mr. KAY: That is a question of argument.

Q. Let's take this situation, Mr. Hill. Supposing this dividend had been declared on the first of the year, we will say on one day, and on the same day of the succeeding week the corporation went out and bought this stock of Lord's for the purpose of redemption. Would it change your mind any as to the character of this payment to Lord? That is Lord and Black got together and Black said to Lord, "You can take your 60% of the surplus out of here," then the corporation deals with Lord and pays him \$60,000., the original contribution, a week hence?

Mr. ADAMS: When Mr. Hill spoke of the division of the earnings, do you mean a division to one or prorata to all the stockholders?

A. Prorata to all the stockholders.

Q. As I understand, that is part of your mental processes in answering Mr. Kay was that this

(Testimony of Harold C. Hill.)

distribution of profits is equal among all the [214] stockholders of the corporation in accordance with their holdings?

A. Yes.

Mr. KAY: I object to this line of cross-examination which Judge Peters is going into. It is something that did not occur. We should confine ourselves to facts before the Board as to what did occur. These suppositious cases have no bearing on the facts as they already exist, and the application of law to those facts. We submit these suppositious cases have no bearing on the issues before this Board.

Mr. PETERS: I think Mr. Hill is trying to assist this Board, and my questions are put with the endeavor to assist this Board.

Mr. KAY: Judge Peters is presenting certain hypothetical situations. Those situations are not complete. He is not stating why this procedure was not followed. He is not giving reasons why E. J. Lord did not obtain a distribution along the lines as proposed by him. In other words, we are only being given a piece-meal hypothetical situation in each case, hence I urge again that this line of examination is of no help to the Board.

Mr. ADAMS: It is rather illuminating, I think.

Q. Let's assume something. Let's assume that legally a dividend can be paid to one stockholder by agreement between himself and all the other [215] stockholders. Assuming that is the law, would

(Testimony of Harold C. Hill.)

you change your opinion as to the assessability under the Territorial income tax law of any of the consideration paid to Mr. Lord?

Mr. KAY: Objected to as not based on any evidence in this case.

Q. You have never run against a dividend paid to one stockholder by agreement of the other stockholders?

A. No.

Q. You have never run against a case such as this, which by agreement of all the stockholders one stockholder gets his share of the surplus and he is clean out and the stock redeemed?

A. No, I don't know such a case.

Questions by Mr. Wrenn:

Q. And before you would have made an assessment in a case of this kind, you would have got an opinion from the Attorney-General's Department as to the law, would you not?

Mr. KAY: Objected to as immaterial.

The CHAIRMAN: Objection sustained.

Redirect Examination by Harold T. Kay, Esq.

Q. You referred to the case of Mineral Products and stated there had been plenty of losses. Were those losses claimed as losses by holders of the stock in Mineral Products in income tax returns made by [216] the stockholders?

A. As I recall, it was optional with the stockholders of Mineral Products whether they should

(Testimony of Harold C. Hill.)

surrender their stock for Magnesia Products or simply drop out of the picture. Those who took the Magnesia Products stock in exchange were not permitted to take a loss at that time. Those who dropped out naturally were given the benefit of the loss, that is the difference between what they paid for the stock and the total loss.

Q. In other words, they claimed losses which were allowed?

A. Yes.

Mr. KAY: That is the case for the Government.

Mr. WRENN: We reserved the right to examine Mr. Buchholtz on redirect. Evidently you don't care to recall him, but there are a few questions we should like to ask him.

GEORGE BUCHHOLTZ,

a witness for the Taxpayer, was recalled for further examination, and testified as follows:

Redirect Examination by Heaton L. Wrenn, Esq.

Q. You were asked on your cross examination by Mr. Kay whether there were any other dividends declared during the year 1930 other than the \$125,000, dividend [217] he called your attention to, and you said "no," in answer to that question. At my

(Testimony of George Buchholtz.)

request since that time have you refreshed your recollection on what occurred during that year?

A. Yes, I have.

Q. And after having refreshed your recollection, what is your answer to that question?

A. There was a dividend declared, but in my answer before I thought it was declared in 1931.

Q. And you have found that was declared in 1930?

A. Yes.

Q. What was the amount of that dividend and to whom was it paid?

A. Paid to Mr. Lord. I don't remember the amount now. It is in the minute book.

Q. A copy of which is on file and admitted in evidence?

A. Yes.

Recross Examination by Harold T. Kay, Esq.

Q. Will you refer to such records as may appear here in evidence in this case and show wherein there was a dividend paid to Mr. Lord in 1930 and where the same appears in the records,—referring to what document do you base that statement of yours on?

A. I don't know what you mean on what document?

Q. You just made the statement on direct examination [218] that upon a reexamination of the records of your company you found that a dividend had been paid to Mr. Lord in 1930 other

(Testimony of George Buchholtz.)

than dividends referred to by you the other day?

A. In the minute book.

Q. I will ask you to refer to the records here in this case, and ask you to point out wherein it appears that a dividend was paid to Mr. Lord?

A. I am talking about a liquidating dividend. The word "dividend" does not apply from the reading of the language.

Mr. ADAMS: "Apply" or "appear"?

A. Does not appear.

Q. What does appear?

A. The first item here on the minutes of final settlement of E. J. Lord, the minutes of December 20, 1930.

Q. What appears there?

A. "Mr. E. E. Black moved that as Mr. E. J. Lord was willing to sell all his stock of E. J. Lord, Limited, the company was to redeem the 600 shares for which the company have to pay for the said shares in the following manner: (1) A sum of money equal to 60% of the net worth of the company as of December 31, 1929. (2) A sum of money equal to 60% of the net profits of all contracts awarded and not completed on December 31, 1929. (3) A sum of money equal to 40% of the amount to which Mr. E. J. Lord [219] may become liable for Federal and Territorial income taxes upon income accrued and to accrue to him resulting from the sale of said 600 shares.

(Testimony of George Buchholtz.)

Mr. Lord agreed to give the company an option to purchase the above-mentioned stock to February 28, 1930, and to have an agreement drawn, signed by above parties, covering the above option, price and payments to be made, a copy of such agreement to be entered into the minute book. Mr. George Buchholtz seconded the motion which was carried unanimously.

Mr. Buchholtz moved that the company upon the exercise of the option cause its Articles of Association to be amended so that the name does not contain the name of 'E. J. Lord' or any words similar to that name."

Q. Does there appear in anything you have read a statement that a dividend had been paid to Mr. E. J. Lord?

A. Yes, by redemption of the stock.

Q. Was there anything specifically stated to the effect that a dividend had been paid to Mr. E. J. Lord?

A. No, the word "dividend" does not appear.

Q. That is the record of your company that you examined on reexamination and upon which you base your statement that a dividend had been paid to Mr. Lord in 1930?

A. That and the final settlement here. [220]

Q. What is that?

A. This is what I was referring to.

Q. Referring to what?

A. The company was to redeem the 600 shares.

(Testimony of George Buchholtz.)

Q. What document are you referring to?

A. Minutes of December 7, 1929.

Q. Entitled Taxpayers' Exhibit 38A?

A. That is right.

Q. Will you point out wherein that term "dividend" appears?

A. I said the word "dividend" does not appear.

Q. So when you used the term "dividend" in your direct examination in response to Mr. Wrenn's question, you were in error in using the term "dividend" were you not?

Mr. WRENN: Objected to as argumentative.

A. I didn't call that an error. I was referring to the liquidating dividend of these 600 shares.

Q. Then you want to qualify your original statement to mean that when you used the term "dividend" you mean "liquidating dividend," is that correct?

A. I suppose so.

Q. Referring to your trial balances, will you state whether in any of the trial balances in evidence in this case for the year 1930 there appears any statement showing that any dividends had been paid by E. J. Lord, Limited, other than the amount of \$25,000. in the year 1930? [221]

A. No; not under the heading of "dividends."

Reredirect Examination by Emil C. Peters, Esq.

Q. Your books do show the distribution to Mr. Lord of 60% of the surplus?

A. Yes, sir.

(Testimony of George Buchholtz.)

Q. And it was that that you refer to as a dividend?

A. Yes.

Rerecross Examination by Harold T. Kay, Esq.

Q. Is it not a fact that this distribution, that Judge Peters calls it, of 60% of the surplus is designated as payment or settlement for stock sold by Mr. E. J. Lord to E. J. Lord, Limited?

A. I would like to answer that question again. As this arose we first started paying Mr. Lord the final payment of \$250,000. It was in 1929, and a further payment was made a few months later upon the completion of the Louis Hind's job, and a third amount couldn't be paid until all these contracts were wound up. At the end of 1930 we had to have some sort of a temporary entry and that heading was called "E. J. Lord stock purchase account" in our books. I took this thing up at times with our auditor and I was first going to put the thing on the suspense account, because it was nothing but a temporary thing until the stock should be redeemed and the final payment was made.—
[222]

No. 2052

In the Supreme Court of the Territory of Hawaii

ON APPEAL FROM THE TERRITORIAL
BOARD OF EQUALIZATION.

In the Matter of the Income Tax Appeal of

EDMUND J. LORD

for the year ending December 31, 1930, First Taxa-
tion Division.

PETITION FOR APPEAL

and

AFFIDAVIT

[Endorsed]: Filed April 4, 1934 at 2:20 o'clock
P. M. Robert Parker, Jr., Clerk Supreme Court.

ROBERTSON & CASTLE,

312 Castle & Cooke Bldg.,

Honolulu, T. H.,

Attorneys for Petitioner.

[223]

[Title of Court and Cause.]

PETITION FOR APPEAL

To the Honorable Chief Justice and Associate Jus-
tices of the Supreme Court of the Territory of
Hawaii:

Comes now EDMUND J. LORD by his attorneys,
Robertson & Castle, and deeming himself aggrieved
by the decision and judgment of the above entitled
court in the above entitled cause, which judgment

was made and entered on the 25th day of January, 1934, pursuant to the opinion of the court theretofore rendered, and claiming that there are manifest and material errors to the damage of said Edmund J. Lord, which errors are specifically set forth in the assignment of errors filed herewith, to which reference is hereby made, respectfully prays that an appeal may be allowed him in the above entitled cause and that he be allowed to prosecute said appeal to the United States Circuit Court of Appeals for the Ninth Circuit in accordance [224] with the statutes in such cases made and provided; and your petitioner prays that an order be made fixing the amount of the bond to be given upon such appeal.

And your petitioner further prays that the Clerk of the Supreme Court of the Territory of Hawaii be directed to send to the United States Circuit Court of Appeals for the Ninth Circuit, a transcript of the record, proceedings and papers in this cause, together with the evidence and exhibits taken herein, all duly authenticated, for the correction of the errors so complained of, and that a citation may issue.

Your petitioner further shows that the decision and judgment of the above entitled cause was rendered in an appeal from the Territorial Board of Equalization, and that the value in controversy, ex-

clusive of interest and costs, exceeds \$5,000, as appears by the record herein.

Dated: Honolulu, T. H., this 4th day of April, 1934.

ROBERTSON & CASTLE,
By NORMAN NEWMARK,
Attorneys for Petitioner.

[225]

[Title of Court and Cause.]

AFFIDAVIT

Territory of Hawaii

City and County of Honolulu—ss.

ALFRED L. CASTLE, being first duly sworn, deposes and says that he is a member of the firm of Robertson & Castle, attorneys for the above named Edmund J. Lord, and duly authorized to make this affidavit on his behalf; that he has read the foregoing Petition for Appeal, knows the contents thereof; that the matters and things therein set forth are true; and that the value in controversy in the above entitled matter exceeds \$5,000, exclusive of interest and costs.

ALFRED L. CASTLE.

Subscribed and sworn to before me this 4th day of April, 1934.

[Seal]

FLORENCE LEE,
Notary Public, First Judicial Circuit,
Territory of Hawaii.

[226]

[Title of Court and Cause.]

ASSIGNMENT OF ERRORS

[Endorsed]: Filed April 4, 1934 at 2:20 o'clock
P. M. Robert Parker, Jr., Clerk Supreme Court.

ROBERTSON & CASTLE,

312 Castle & Cooke Bldg.,

Honolulu, T. H.

Attorneys for Edmund J. Lord.

[227]

[Title of Court and Cause.]

ASSIGNMENT OF ERRORS

Comes now the above named Edmund J. Lord and files the following assignment of errors upon which he will rely in the prosecution of the appeal herewith petitioned for in the said cause to the United States Circuit Court of Appeals for the Ninth Circuit from the judgment of this court made and entered on the 25th day of January, 1934.

Assignment No. 1

The Supreme Court of the Territory erred in failing to rule that that part of the consideration received by Edmund J. Lord for the transfer of his stock to E. J. Lord, Limited, over and above his original capital contribution, which represented his theretofore undivided interest in the accumulated earnings, profits and surplus of said corporation, and which was paid out of such earnings, profits and surplus, upon which a [228] Territorial income tax

had been assessed and paid, was received as dividends and was exempt from taxation under the provisions of Section 1391, R. L. 1925.

Assignment No. 2

The Supreme Court of the Territory erred in failing to rule that that part of the consideration received by Edmund J. Lord for the transfer of his stock to E. J. Lord, Limited, over and above his original capital contribution, which was paid out of accumulated corporate earnings, profits and surplus upon which a territorial income tax had been assessed and paid, was exempt from taxation under the provisions of Section 1391, R. L. 1925.

Assignment No. 3

If some part of the consideration received by said Edmund J. Lord for the transfer of his stock to E. J. Lord, Limited, was subject to taxation despite the provisions of Section 1391, Revised Laws, 1925, then the Supreme Court of the Territory of Hawaii erred in failing to rule that the tax could be assessed only on the difference between the value of said stock as of January 1, 1930, and the amount which he received therefor.

WHEREFORE, said Edmund J. Lord prays that the judgment of the Supreme Court of the Territory of Hawaii be reversed and the cause remanded with directions to set aside the proposed assess-

ment, and for such other or further orders or relief as to the Court may seem just and proper.

Dated: Honolulu, T. H., this 4th day of April, 1934.

ROBERTSON & CASTLE,

Attorneys for Edmund J. Lord.

Service of a copy of the foregoing assignment of errors is hereby admitted this 4th day of April, 1934.

H. R. HEWITT,

Attorney General.

[229]

[Title of Court and Cause.]

ORDER ALLOWING APPEAL AND FIXING
AMOUNT OF BOND

[Endorsed]: Filed April 4, 1934 at 2:45 o'clock
P. M. Robert Parker, Jr., Clerk Supreme Court.

[230]

[Title of Court and Cause.]

ORDER ALLOWING APPEAL AND FIXING
AMOUNT OF BOND

The petition of Edmund J. Lord for an appeal to the United States Circuit Court of Appeals for the Ninth Circuit, dated the 4th day of April, 1934, from the final judgment of this Court dated the 25th day of January, 1934, is hereby granted and the appeal is allowed; and the amount of the bond is hereby fixed in the sum of \$250.00.

Dated: Honolulu, T. H., this 4th day of April, 1934.

[Seal]

ANTONIO PERRY,
Chief Justice, Supreme Court of the
Territory of Hawaii. [231]

[Title of Court and Cause.]

CITATION ON APPEAL

[Endorsed]: Filed April 4, 1934 at 3:00 o'clock
P. M. Robert Parker, Jr., Clerk Supreme Court.
[232]

[Title of Court and Cause.]

CITATION ON APPEAL

To THE TERRITORY OF HAWAII and
HARRY R. HEWITT, its Attorney General:
GREETING:

You are hereby cited and admonished to be and appear in the United States Circuit Court of Appeals for the Ninth Circuit, to be held in the City of San Francisco, State of California, within thirty days from the date hereof, pursuant to an order allowing an appeal from the Supreme Court of the Territory of Hawaii in a suit wherein Edmund J. Lord is appellant, to show cause, if any there be, why the judgment rendered against said appellant should not be corrected and why speedy justice should not be done to the said appellant on that behalf.

WITNESS the Honorable Charles Evans Hughes, [233] Chief Justice of the Supreme Court of the United States of America, this 4th day of April, 1934.

[Seal]

ANTONIO PERRY,
Chief Justice, Supreme Court of the
Territory of Hawaii.

Receipt of a copy of the foregoing Citation is hereby admitted this 4th day of April, 1934.

H. R. HEWITT,
Attorney General of the Territory of Hawaii.
[234]

[Title of Court and Cause.]

BOND ON APPEAL

[Endorsed]: Filed April 4, 1934 at 2:46 o'clock
P. M. Robert Parker, Jr., Clerk Supreme Court.

[235]

[Title of Court and Cause.]

BOND ON APPEAL

KNOW ALL MEN BY THESE PRESENTS:
That EDMUND J. LORD, as Principal, and
UNITED STATES FIDELITY AND GUARAN-
TY COMPANY, as Surety, are held and firmly
bound unto THE TERRITORY OF HAWAII in
the full and just sum of Two Hundred and Fifty
Dollars (\$250.00) to be paid to the said The Terri-
tory of Hawaii, to which payment, well and truly to

be made, the above named parties bind themselves, their respective heirs, executors, administrators, successors and assigns, firmly by these presents.

WHEREAS, in the above entitled cause and Court, an appeal from the judgment heretofore therein rendered has been taken and allowed to the United States Circuit Court of Appeals for the Ninth Circuit,

NOW, THEREFORE, if the said principal shall [236] prosecute said appeal with effect and pay all costs if he fails to sustain said appeal, then this obligation shall be void; otherwise it shall remain in full force and effect.

IN WITNESS WHEREOF the said EDMUND J. LORD, Principal, and UNITED STATES FIDELITY AND GUARANTY COMPANY, Surety, have caused these presents to be executed this 4th day of April, 1934.

(Signed) EDMUND J. LORD,

Principal.

UNITED STATES FIDELITY AND
GUARANTY COMPANY,

[Seal] By HERMAN LUIS,
Its Attorney-in-Fact,
Surety.

Approved as to form and amount of bond and sufficiency of surety.

[Seal] (Signed) ANTONIO PERRY,
Chief Justice, Supreme Court of
the Territory of Hawaii. [237]

[Title of Court and Cause.]

PRAECIPE

[Endorsed]: Filed April 4, 1934 at 3:01 o'clock
P. M. Robert Parker, Jr., Clerk Supreme Court.

ROBERTSON & CASTLE,

312 Castle & Cooke Bldg.,

Honolulu, T. H.,

Attorneys for Edmund J. Lord.

[238]

[Title of Court and Cause.]

PRAECIPE

To ROBERT PARKER, ESQUIRE, Clerk of the
Supreme Court of the Territory of Hawaii:

You will please prepare a transcript of the record
in the above entitled cause to be filed in the office
of the Clerk of the United States Circuit Court of
Appeals for the Ninth Circuit and include in said
transcript the following:

1. Territorial income tax return of E. J. Lord
dated June 18, 1931, together with notice of change
of assessment dated June 19, 1931 pasted thereon,
and schedule attached thereto;

2. Notice of Appeal from Assessment dated June
18, 1931;

3. All exhibits;

4. Transcript of evidence taken before the Board
of Equalization, excluding therefrom the arguments
of counsel beginning on page 194 and continuing to
the end;

5. Decision of the Territorial Board of Equal-
ization dated the 20th day of January, 1932; [239]

6. Appeal and Notice of Appeal dated January 29, 1932, from the Territorial Board of Equalization to the Supreme Court of the Territory of Hawaii;

7. Affidavit of Charles T. Wilder, Chairman of the Board of Equalization, dated February 1, 1932;

8. Decision of the Supreme Court of the Territory of Hawaii, dated the 2nd day of December, 1933;

9. Judgment of the Supreme Court of the Territory of Hawaii, dated January 25, 1934;

10. Petition for appeal and affidavit;

11. Assignment of errors;

12. Order allowing appeal and fixing amount of bond;

13. Citation;

14. Bond on appeal;

15. This praecipe;

16. All orders enlarging time to docket cause.

You will annex to and transmit with the record the original citation issued in said cause, originals of all orders enlarging time to docket cause and your certificate under seal stating in detail the cost of the record and by whom paid, in compliance with Rule 14 of the United States Circuit Court of Appeals for the Ninth Circuit.

Dated: Honolulu, T. H., this 4th day of April, 1934.

(s) ROBERTSON & CASTLE,
Attorneys for Edmund J. Lord.

Service of a copy of the foregoing Praeceptum is hereby admitted this 4th day of April, 1934.

(s) H. R. HEWITT,

Attorney General of the Territory of Hawaii.

[240]

[Title of Court and Cause.]

ORDER ENLARGING TIME TO FILE
RECORD AND DOCKET CAUSE

[Endorsed]: Filed April 20, 1934 at 2:30 o'clock
P. M. Robert Parker, Jr., Clerk Supreme Court.

[241]

[Title of Court and Cause.]

ORDER ENLARGING TIME TO FILE
RECORD AND DOCKET CAUSE

Upon the application of Appellant above named,
and good cause appearing therefor,

IT IS HEREBY ORDERED, pursuant to Section 1 of Rule 16 of the United States Circuit Court of Appeals for the Ninth Circuit, that Appellant above named and the Clerk of this Court be and they are hereby allowed up to and including the 2nd day of June, 1934, within which to file the record and transcript and docket said cause with the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

Dated: Honolulu, T. H., April 20, 1934.

[Seal]

ANTONIO PERRY,
Chief Justice, Supreme Court of the
Territory of Hawaii.

Attest:

ROBERT PARKER, JR.,
Clerk.

[242]

[Title of Court and Cause.]

ORDER ENLARGING TIME TO FILE
RECORD AND DOCKET CAUSE

[Endorsed]: Filed May 12, 1934 at 10:30 o'clock
A. M. Robert Parker, Jr., Clerk Supreme Court.

[243]

[Title of Court and Cause.]

ORDER ENLARGING TIME TO FILE
RECORD AND DOCKET CAUSE

Upon the application of Appellant above named,
and good cause appearing therefor,

IT IS HEREBY ORDERED, pursuant to Section 1 of Rule 16 of the United States Circuit Court of Appeals for the Ninth Circuit, that Appellant above named and the Clerk of this Court be and they are hereby allowed up to and including the 15th day of July, 1934, within which to file the record and transcript and docket said cause with the Clerk

of the United States Circuit Court of Appeals for
the Ninth Circuit.

Dated: Honolulu, T. H., May 12th, 1934.

[Seal]

A. PERRY,

Chief Justice, Supreme Court of the
Territory of Hawaii.

Approved:

W. B. PITTMAN,
Attorney General.

Attest:

ROBERT PARKER, JR.,
Clerk.

[244]

[Title of Court and Cause.]

STIPULATION AS TO CONTENTS OF
TRANSCRIPT OF RECORD

[Endorsed]: Filed June 28, 1934 at 9:00 o'clock
A. M. Robert Parker, Jr., Clerk Supreme Court.

WILLIAM B. PITTMAN,
Attorney General,
Honolulu, Territory of
Hawaii.

ROBERTSON & CASTLE,
312 Castle & Cooke Bldg.,
Honolulu, T. H. [318]

[Title of Court and Cause.]

STIPULATION AS TO CONTENTS OF
TRANSCRIPT OF RECORD

IT IS HEREBY STIPULATED AND AGREED by and between the TERRITORY OF HAWAII, appellee, and EDMUND J. LORD, appellant, that the transcript of record to be certified to and filed in the United States Circuit Court of Appeals for the Ninth Circuit, pursuant to the appeal heretofore allowed herein, shall exclude the following exhibits:

Tax Assessor's Exhibit "A";

Tax Payers' Exhibits 1, 2, 4, 6-a, to 6-f, 7, 8-a-b-c, 10, 11, 12, 13, 17, 32 and 36.

IT IS FURTHER STIPULATED that the Clerk of Court shall omit the aforesaid exhibits from the record to be filed on appeal without the necessity of the filing of an amended praecipe, and that this stipulation shall take effect upon the approval thereof by Honorable Antonio Perry, Chief Justice of the above entitled court, or upon the approval of either of the Associate Justices thereof.

Dated: Honolulu, T. H., this 27 day of June, 1934.

TERRITORY OF HAWAII,
By MONTGOMERY E. WINN,
Its First Deputy Attorney
General.

EDMUND J. LORD,
By ROBERTSON & CASTLE,
His Attorneys.

Approved:

[Seal]

ANTONO PERRY,
Chief Justice, Supreme Court
of Hawaii.

[Title of Court and Cause.]

CLERK'S CERTIFICATE.

Territory of Hawaii

City and County of Honolulu—ss.

I, ROBERT PARKER, JR., Clerk of the Supreme Court of the Territory of Hawaii, by virtue of the petition for appeal filed April 4, 1934, the original whereof is attached to the foregoing transcript of record, being pages 223 to 226, both inclusive, and in pursuance to the praecipe filed April 4, 1934, copy whereof is attached to the foregoing transcript of record, being pages 238 to 240, both inclusive, and in pursuance to the stipulation filed June 28, 1934, the original whereof is attached to the foregoing transcript of record, being pages 318 to 319, both inclusive.

DO HEREBY TRANSMIT to the Honorable United States Circuit Court of Appeals for the Ninth Circuit, the foregoing transcript of record, being pages 1 to 222, both inclusive, pages 235 to 237, both inclusive, pages 245 to 317 both inclusive, and I CERTIFY the same to be full, true and correct copies of the record, entries, opinions, minutes, exhibits and final judgment, which are now on file in the office of the Clerk of the Supreme Court of the Territory of Hawaii, in the above entitled cause, Supreme Court No. 2052.

I DO FURTHER CERTIFY that the original assignment of errors, filed April 4, 1934, with acknowledgment of service of a copy by H. R. Hewitt,

Attorney General, being pages 227 to 229, both inclusive, the original order allowing appeal and fixing amount of bond, filed April 4, 1934, being pages 230 to 231, both inclusive, the original citation on appeal, filed April 4, 1934, with acknowledgment of service of a copy thereof by H. R. Hewitt, Attorney General, being pages 232 to 234, both inclusive of the foregoing transcript of record, are herewith returned.

I LASTLY CERTIFY that the cost of the foregoing transcript of record is \$160.55, and the said amount has been paid by Messrs. Robertson & Castle, attorneys for E. J. Lord. [320]

IN TESTIMONY WHEREOF, I have hereunto set my hand and affixed the seal of the Supreme Court of the Territory of Hawaii, at Honolulu, City and County of Honolulu, Territory of Hawaii, this 29th day of June, 1934.

[Seal]

ROBERT PARKER, JR.,
Clerk of the Supreme Court of the
Territory of Hawaii. [321]

No. 7543

In the United States Circuit Court of Appeals for
the Ninth Circuit.

APPEAL FROM THE SUPREME COURT OF
THE TERRITORY OF HAWAII
EDMUND J. LORD,

Appellant,

vs.

TERRITORY OF HAWAII,

Appellee.

STIPULATION AS TO PRINTING OF
RECORD

ROBERTSON & CASTLE,
312 Castle & Cooke Bldg.,
Honolulu, T. H.,

Attorneys for Appellant.

WILLIAM B. PITTMAN, ESQ.,
Attorney General,
Territory of Hawaii,

Attorney for Appellee.

[Title of Court and Cause.]

STIPULATION AS TO PRINTING OF
RECORD

IT IS HEREBY STIPULATED by and between the respective parties hereto, that in printing the record in the above entitled cause, the Clerk shall omit therefrom the following documents and papers:

Tax Assessor's Exhibits B to B-14, inclusive, being photostatic copies of trial balances of E. J. Lord, Limited, (or E. E. Black, Limited), for the months of November and December, 1929, and for the months of January to December 1930, said exhibits being found on pages —— to —— in the transcript of record certified to the above entitled court by the Clerk of the Supreme Court of the Territory of Hawaii;

Taxpayers' Exhibits 18 to 22, inclusive, being territorial income tax returns of E. J. Lord, Limited, for income earned during the years 1926 to 1929, inclusive, and of E. E. Black, Limited, for income earned during the year 1930, said exhibits being found on pages —— to —— in the transcript of record certified to the above entitled court by the Clerk of the Supreme Court of the Territory of Hawaii; and

Taxpayers' Exhibits 23 to 27, inclusive, being receipts for income taxes paid by E. J. Lord, Limited, and E. E. Black, Limited, for income earned during the years 1926 to 1930, inclusive, said exhibits being found on pages —— to —— in the

transcript of record certified to the above entitled court by the Clerk of the Supreme Court of the Territory of Hawaii.

Dated: Honolulu, T. H., this 27th day of June, 1934.

TERRITORY OF HAWAII,
By MONTGOMERY E. WINN,
Its First Deputy Attorney
General.

EDMUND J. LORD,
By ROBERTSON & CASTLE,
His Attorneys.

Approved:

ANTONIO PERRY,
Chief Justice of the Supreme Court
of the Territory of Hawaii.

Justice of the United States Court
of Appeals for the Ninth Circuit.

[Endorsed]: Filed July 6, 1934. Paul P. O'Brien,
Clerk.

[Endorsed]: No. 7543. United States Circuit Court of Appeals for the Ninth Circuit. Edmund J. Lord, Appellant, vs. Territory of Hawaii, Appellee. Transcript of Record. Upon Appeal from the Supreme Court of the Territory of Hawaii.

Filed July 6, 1934.

PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of Appeals
for the Ninth Circuit.

IN THE

United States Circuit Court of Appeals

FOR THE

Ninth Circuit

EDMUND J. LORD,	}
Appellant,	
vs.	
TERRITORY OF HAWAII,	
Appellee.	}

UPON APPEAL FROM THE SUPREME COURT OF
THE TERRITORY OF HAWAII

BRIEF FOR APPELLANT

ROBERTSON & CASTLE
A. L. CASTLE
N. M. NEWMARK

Castle & Cooke Building
Honolulu, T. H.

Attorneys for Appellant

FILED

FEB 14 1935

PAUL F. DUNN

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No. 7543

IN THE
United States Circuit Court of Appeals
FOR THE
Ninth Circuit

EDMUND J. LORD,	}
Appellant,	
vs.	
TERRITORY OF HAWAII,	}
Appellee.	

BRIEF FOR APPELLANT

STATEMENT OF THE CASE

This is an appeal from a judgment of the Supreme Court of the Territory of Hawaii, which affirmed a decision of the Territorial Board of Equalization, sustaining an assessment against the appellant of an income tax for the year 1930 on certain moneys received by him during the year preceding January 1, 1931.

A succinct summary of the undisputed facts is found in the decision of the Supreme Court (32 Haw. 896 at 897-898; Record pp. 24-25), and statements having no record reference are taken therefrom.

E. J. Lord and E. E. Black, having been prior thereto associated in the contracting and building business, in September, 1926, formed a corporation under the name of E. J. Lord, Limited. The corporation had a capital stock of \$100,000 divided into 1000 shares, 600 shares of which were issued to E. J. Lord and 400 shares to E. E. Black, each contributing in payment of the stock money or other capital of the value of \$60,000 and \$40,000 respectively. To comply with legal requirements three other stockholders were named, each as the holder of one share, but these were only nominal or "dummy" shareholders (Rec. p. 202), and in each of the annual reports subsequently filed with the Treasurer of the Territory only Lord and Black were named as shareholders.

The corporation met with a large measure of success and received substantial profits from its operations (Rec. p. 24; see Ex. 28 A, p. 104). At the end of each year the corporation closed its books and determined its profit and loss with the exception of contracts then pending—the credit balance, if any, being then transferred to surplus (Rec. p. 102). The profits so determined were regularly returned in the income tax returns of the corporation, and Territorial income taxes paid thereon (Rec. pp. 106-107).

Late in 1929 the appellant, E. J. Lord, because of ill health, desired to retire from the active pursuit of the business and he and Black began negotiations looking toward the retirement of the former (Rec. p. 56). In consultation with the attorney for E. J. Lord, Limited, E. C. Peters, Esquire, a former Chief Justice of the Territorial Supreme Court, it was agreed, primarily,

that Lord would receive for his stock his original capital contribution (\$60,000), plus his share (60%) of the undivided profits (Rec. pp. 57-58), Black's intention being to retire Lord's stock and reduce the capital stock of the corporation to \$40,000 thereafter (Rec. pp. 57, 201).

On December 7, 1929, the board of directors of E. J. Lord, Limited, approved the proposal that the corporation redeem the stock of E. J. Lord as planned (Ex. 38 A, Rec. p. 134), and on December 13, 1929, a formal written agreement, giving the corporation an option to redeem the stock, was executed (Ex. 9, Rec. p. 65). This agreement was not with Black but was solely with the corporation, and gave it the right to redeem Lord's stock upon the payment to him of:

(a) A sum of money equal to 60% of the net worth of the company as of December 31, 1929;

(b) A sum of money equal to 60% of the net profits of contracts awarded but not completed on December 31, 1929; any losses to be shared 60-40.

(c) A sum of money equal to 40% of the Territorial and Federal income taxes Lord might become liable to pay as a result of the transaction.

In accordance with the prior action of the board of directors the option was duly accepted.

Sixty per cent of the net worth of the corporation, as of December 31, 1929, was found to be \$273,855.36, and pursuant to the option agreement \$250,000 was paid on account on February 15, 1930 (Ex. 15, Rec. p. 83), the balance being paid later in the year (Ex. 35, Rec. p. 124). The contracts which were not completed

on December 31, 1929, were all completed in 1930 and final payment to Lord was made prior to the end of that year (Ex. 16, Rec. p. 90), with the exception of a payment of \$20,328.50 for his Federal tax liability which was paid early in 1931 (Ex. 29, 30, 35, Rec. pp. 108, 110, 124). Immediately after this latter payment the capital stock of the corporation was reduced to \$40,000 (Rec. pp. 119-120).

The total amount paid Lord was \$468,219.98, \$60,000 of which, representing Lord's original capital contribution, was paid by the corporation out of capital account and the remainder, or \$408,219.98, representing Lord's 60% interest in the profits and the surplus of the corporation (but including the sum of \$20,328.50, being 40% of Lord's Federal income tax liability), being paid out of surplus (Rec. pp. 115-117).

With respect to that \$408,219.98 the Territorial Supreme Court said:

"It is undisputed that the money paid to E. J. Lord under the contract referred to, other than the sum of \$60,000 which came from capital, was actually paid by the corporation out of undivided profits, partly earned prior to the date of the contract and partly earned after the date of contract and that upon all of these undivided profits the corporation had paid the tax of 2% required by law." (Rec. p. 26; 32 Haw. at 898.)

Section 1391, R. L. of Hawaii 1925, which is part of Chapter 103, relating to income taxes, provides that:

". . . in assessing the income of any person or corporation there shall not be included *the amount*

*received from any corporation as dividends** upon the stock of such corporation if the tax of two per centum has been assessed upon the net profits of such corporation as required by this chapter, . . .”

Accordingly, in the Territorial income tax return of E. J. Lord for the year 1930, prepared by Mr. H. W. Camp, a tax expert and expert accountant (Rec. p. 145), the sum of \$406,569.98 (being \$468,219.98 less the \$60,000 capital, less a deductible attorneys’ fee of \$1650 in connection with the transaction), was returned as exempt from taxation as an “amount received . . . as dividends” within the meaning of the above section (Rec. p. 2).

The tax assessor took the view that the transaction was merely an ordinary purchase and sale of stock—just as if Lord had sold his stock to a third person—and levied an assessment on said \$406,569.98 as being the net gain derived from the sale of the stock. As a result of this additional assessment the net taxable income of the appellant for the year 1930 was determined to be \$398,224.40, and a tax was levied thereon in the sum of \$18,686.22 (Rec. pp. 4, 14).

The Board of Equalization—a tax board composed entirely of laymen—sustained the assessment and on appeal to the Supreme Court that decision was affirmed.

SPECIFICATIONS OF ERROR

The appellant relies upon each of the assignments of error filed with his petition for appeal (Rec. p. 282), which are here set forth:

*All emphasis supplied by us unless otherwise noted.

ASSIGNMENT NO. 1

The Supreme Court of the Territory erred in failing to rule that that part of the consideration received by Edmund J. Lord for the transfer of his stock to E. J. Lord, Limited, over and above his original capital contribution, which represented his theretofore undivided interest in the accumulated earnings, profits and surplus of said corporation, and which was paid out of such earnings, profits and surplus, upon which a Territorial income tax had been assessed and paid, was received as dividends and was exempt for taxation under the provisions of Section 1391, R. L. 1925.

ASSIGNMENT NO. 2

The Supreme Court of the Territory erred in failing to rule that that part of the consideration received by Edmund J. Lord for the transfer of his stock to E. J. Lord, Limited, over and above his original capital contribution, which was paid out of accumulated corporate earnings, profits and surplus upon which a territorial income tax had been assessed and paid, was exempt from taxation under the provisions of Section 1391, R. L. 1925.

ASSIGNMENT NO. 3

If some part of the consideration received by said Edmund J. Lord for the transfer of his stock to E. J. Lord, Limited, was subject to taxation despite the provisions of Section 1391, R. L. 1925, then the Supreme Court of the Territory of Hawaii erred in failing to rule that the tax could be assessed only on the difference between the value of said stock as of January 1, 1930, and the amount which he received therefor.

Assignments Nos. 1 and 2 will be argued under the same general heading. Under Assignment No. 2 it is contended that the entire amount of \$406,569.98 (being \$408,219.98 less the admitted deduction of \$1650) is exempt from taxation, while under Assignment No. 1 it is contended that at least \$386,241.48 (or \$406,569.98 less \$20,328.50—the latter sum being the amount paid for Lord's Federal tax liability) is so exempt.

ANALYSIS OF THE CASE

There can be no question as to the purpose of Section 1391. A state can levy an income tax on the profits of a corporation, and then tax the stockholders again when those same profits are distributed to them by the corporation. Obviously Section 1391 was passed to prohibit this form of "double taxation"—to use the term loosely—and to definitely provide that where a corporation had paid the tax on its profits those same profits, when distributed to the stockholders, should not again be taxed.

In *Matsons Ford Bridge Co. v. Commonwealth*, 117 Pa. 265, 11 Atl. 813, all of the property and franchise of a corporation was taken by eminent domain and the corporation divided the damages, \$75,000, among its stockholders. The Pennsylvania capital stock tax was measured by dividends. The state levied a tax on the theory that \$30,000—being the excess of \$75,000 over the original capital of \$45,000—was a dividend.

The assessment was sustained, and in the course of its opinion the court said:

“... The design of the act of 1879 is accurately stated by the learned judge of the court below:
‘The theory of the act is that the profits realized

by the corporation, whether directly arising from its operations from year to year, or from the increase in the value of its property from whatever cause, will sooner or later reach the pockets of its stockholders; and that when they do, they furnish a fair measure of the value of the capital stock, and therefore of the amount of tax which it ought to pay.' " (11 Atl. at 814.)

An identical principle applies to the statute under consideration. The theory of Section 1391 is that sooner or later the profits of a corporation will reach the hands of the stockholders, and when they do, they should not again be taxed.

That does not mean that just because profits are paid out to a stockholder they are tax free, nor that there is an exemption only where regularly declared annual "dividends" are paid. The test under the statute is whether the particular amount paid, which may represent either current or accumulated profits, is or is not received "as dividends"—that is, as the stockholder's distributive share of profits. The question in the case at bar is simply whether this transaction was an ordinary sale of stock at a fixed price—in which event the mere fact that part of the consideration was paid out of profits would be immaterial—or whether the undisputed evidence shows that the corporation paid out, and Lord received, a certain amount of money in the transaction as his distributive share of, or 60% interest in, the profits and surplus of the corporation, i.e., "as dividends."

The issue thus delineated was clearly defined in the opinion of the Supreme Court (32 Haw. 898-899; Rec. p. 26), the court in effect conceding the correctness of

the foregoing analysis. It stated, as we have, that the main question was, "What was the nature of the transaction between the corporation and Lord?" (32 Haw. at 899; Rec. p. 27), and that the question of what was actually done was "necessarily in large measure a question of the intention of the parties." (32 Haw. at 904; Rec. p. 33.)

In its decision the Court analyzed the option agreement of December 13, 1929, and the records of the corporation, apparently to determine whether or not there was any reference in the written agreement or records to the distribution in question as a "dividend." Finding none, it ruled in favor of the government on the theory that "irrespective of what the parties might have accomplished if they had pursued a different course, the transaction as it actually occurred was a sale and purchase and resulted in a profit to Lord in the sale of his stock." (32 Haw. at 905, Rec. p. 35.)

Though in effect conceding that formalities were not necessary to have a given distribution be a dividend (*infra* p. 27), the court actually looked at the form of the transaction and disregarded its substance. While admitting that the intention of the parties was controlling, it looked only at the formal documents to see how they had described the transaction and, in so doing, overlooked that:

"A formal resolution is not the only evidence of corporate action. *Young v. U. S. Mortgage & Trust Co.*, 214 N. Y. 269, 108 N. E. 418. Everything that was said and done, the entire setting of the occasion, may help in determining the authorization intended to be conferred and the purpose to be carried out and effected. *Catholic Foreign Mis-*

sion Soc. of America v. Oussani, 215 N. Y. 1, 109 N. E. 80 Ann. Cas. 1917A, 479.” (*In Re Norton’s Will*, 224 N.Y.S. 77 at 87.)

We submit that when that rule is applied, and the setting of the transaction, the intention of the parties, and the circumstances under which this distribution was made are all considered, it will be clearly seen that the transaction was not an ordinary sale of stock at a price supposedly representative of its value, but that part of the consideration paid Lord for his stock was paid to him *as his distributive share of the profits in the corporation*, i.e., “as dividends.”

We should like to make it clear that no question of reviewing conflicting evidence or disturbing any findings of fact is here involved. The facts are undisputed. The question is simply one of determining the intention of the parties from *all* of those facts, rather than confining our inquiry to the form of the transaction and to *some* of the facts.

Nor is any question of “local law,” or local administrative practice here involved. This is the first case of this nature to come before the taxing officials of the Territory and there was no precedent or administrative practice to follow (Rec. pp. 245-246, 272).

Nor is any question of local statutory construction at issue in this case. In its decision the Supreme Court tacitly conceded that the statute in question could cover the type of transaction in question. On the Supreme Court’s own analysis of the problem the question presented is purely and simply: What was the essential character of the transaction in question?—and that is the question which this brief will consider.

But if some question of statutory construction should nevertheless be thought to be involved, we submit that this case would then be governed by *Castle v. Castle*, 267 Fed. 521. There this court refused to be bound by a decision of the Territorial Supreme Court as to whether a dower statute, covering “movable effects in possession,” included insurance proceeds, saying:

“It will be conceded that the Federal courts lean toward the interpretation of a local statute adopted by the local courts; but a question of dower is very broad and clearly of a more general nature than are matters confined merely to local usages.” (267 Fed. at 524.)

If that is true in the case of dower *a fortiori* it applies in a case involving dividends.

ARGUMENT

I.

THE TERRITORIAL COURT ERRED IN DISALLOWING APPELLANT'S CLAIM OF EXEMPTION

(Assignments of Error 1, 2).

A.

PART OF THE CONSIDERATION RECEIVED BY APPELLANT WAS PAID BY THE CORPORATION AND RECEIVED BY HIM AS HIS DISTRIBUTIVE SHARE OF THE PROFITS AND SURPLUS OF THE CORPORATION.

The Background of the Transaction.

Prior to the formation of the corporation appellant was a contractor and Black worked for him on a salary

and profit sharing basis (Rec. p. 202). They formed a corporation in which they owned all the shares (three shares out of the total of 1,000 held but not owned by others purely to qualify them as incorporators can be disregarded). Appellant decided to retire from the business and as a means of withdrawal the two shareholders decided to divide the business in the ratio of ownership by Lord getting back his original capital contribution plus his share, 60%, of the net profits.

Black first saw attorney E. C. Peters, the former Territorial Chief Justice, who was at all times acting for E. J. Lord, Limited (Rec. p. 62), and then discussed the matter with Lord. Thereafter, on December 7, 1929, the board of directors of E. J. Lord, Limited, approved the plan of redeeming Mr. Lord's stock on the terms thereafter set forth in the formal written option of December 11, 1929 (Appellant's Ex. 38-A, Rec. p. 34).

The discussions of Mr. Black and Mr. Lord, relative to the redemption by the corporation of the latter's stock, as stated by attorney E. C. Peters,

“resulted in an agreement between the corporation, on the one hand, and Mr. Lord on the other, that Lord was to receive what he had originally put into the corporation by way of contribution on the original organization, and that he was to also receive the undivided profits, which, with the capitalization, would represent the net worth of the business, and that net worth was to be computed as of the close of the year 1929, December 31st.” (Rec. pp. 57-58.)

Furthermore, as the closing items for the year 1929 would not disclose Lord's interest in the contracts

which the corporation then had pending—the profits on which were not computed until the acceptance of the same by the government—Mr. Lord, consistent with the general scheme to divide the profits in accordance with the respective interests, claimed that he was entitled to a percentage of profits that might accrue from those contracts (Rec. pp. 59-60). This was agreeable to Mr. Black so long as Mr. Lord would agree to share any losses (Rec. p. 60).

To again quote from the testimony of attorney Peters:

“So that on the 11th of December, 1929, at the time that this consultation was had with Mr. Lord and Mr. Black, it was agreed primarily that Mr. Lord was to receive sixty per cent. of the net worth of the business as it was disclosed at the end of the year, and sixty per cent. of the profits that might accrue upon those contracts, a list of which Mr. Buchholtz was to furnish.” (Rec. p. 60.)

The manner in which the parties themselves viewed the transaction is thus set forth in the testimony of Mr. Black:

“Q. And the idea was then to pay Mr. Lord in the matter of the redemption of the stock his capital contribution plus his share of the earnings in the company?

“A. That is quite right, and the contracts pending.” (Rec. p. 201.)

“Q. And in 1929 you desired to own your own business and proposed to Mr. Lord to buy him out?

“A. That’s right. I would not say particularly ‘buy’ because the whole assets of the com-

pany were divided sixty-forty as best we could. I agreed with Mr. Lord to take the plant as he was going out of the contracting business, and that value was established and with the bonds and cash we had that prorated sixty-forty." (Rec. p. 203.)

"It was just a division of the assets of the company, plant, stock, bonds and cash, sixty-forty. That is what it amounted to." (Rec. p. 204.)

The intention of the parties thus disclosed shows that the transaction was to be the very antithesis of an ordinary sale at a fixed price, but included the essential element of a dividend—the distribution of profits as such.

Bearing in mind that the agreement of December 13, 1929, was intended to be a summation of the prior understanding of the parties, we turn to a consideration of that document and of what was done pursuant thereto.

The Agreement of December 13, 1929 (Ex. 9).

This document, after reciting that the corporation, party of the second part, desired to redeem the stock of Mr. Lord, stated that the latter was willing to accept and the former to pay therefor

"A sum of money equal to sixty per cent (60%) of the net worth of the party of the second part as of December 31, 1929, and a sum of money equal to sixty per cent (60%) of the net profits yet to accrue to the party of the second part by its completion of the respective works contemplated by certain executory contracts to which the said party of the second part is a party, remain-

ing uncompleted, and the further sum of money equal to forty per cent (40%) of the amount to which the party of the first part may become liable to the United States of America and/or the Territory of Hawaii for income taxes upon income accrued and/or to accrue to him by reason of and resulting from the exercise by the party of the second part of the option hereby granted and the consummation of the sale of said six hundred (600) shares of the capital stock of said party of the second part." (Rec. pp. 66-67.)

It further provided that as the net worth of the corporation could not be determined until the books had been closed for the year 1929 and an audit made thereof (Rec. p. 67) and as there were certain incompleted contracts with the government (Rec. p. 67), the corporation would cause its books to be closed as of December 31, 1929, and cause the same to be audited, and complete the pending contracts (Rec. p. 69).

The agreement also provided that 60% of the net worth of the corporation as of December 31, 1929, should be paid upon the exercise by the corporation of the option granted in the document, but if that amount exceeded \$250,000 the amount of excess over that sum could be retained until the completion of what was known as the St. Louis Heights contract (Rec. p. 71). It further provided that the 60% of the net profits on incompleted contracts should be paid when the profits therefor were received by the corporation, and that the 40% of the Federal and Territorial income taxes should be paid immediately upon assessment of such taxes (Rec. p. 71).

Under the terms of the agreement Lord was to deliver his stock, endorsed by way of pledge, to the cor-

poration to be held by it as security for the consummation of the deed, the corporation being empowered to cause the stock to be redeemed (Rec. p. 68). A further provision was made for arbitration in case of dispute (Rec. p. 72).

It should be remembered that this agreement was made pursuant to authorization of the board of directors of E. J. Lord, Limited (Ex. 38-A, Rec. p. 134) and therefore every step of the transaction was brought to the attention of and approved by that board (Ex. 38-B, Rec. p. 135; Ex. 38-C, Rec. p. 138; Ex. 37-D, Rec. p. 199; and Ex. 131, Rec. p. 131).

The Consummation of the Deal.

Pursuant to the action of the board of directors on December 7, 1929, the option was duly accepted by the corporation. 60% of the net worth of the corporation, as of December 31, 1929, was determined to be \$273,855.36, and under the terms of the agreement \$250,000 was paid on account on February 15, 1930 (Ex. 15, Rec. p. 83). The final payment, in accordance with the option agreement, was deferred until the completion of the pending contracts.

Upon completion of those contracts and the determination of the profits thereon final payment was made. Appellant's Exhibit 33-A-B (Rec. p. 114) graphically shows the details of the transaction:

TAXPAYER'S EXHIBIT 33-A-B

STATEMENT SHOWING ANALYSIS

OF	\$468,219.98
Distributed to E. J. LORD BY E. J.	
LORD, LTD., OUT OF CAPITAL AND	
SURPLUS.	

Surplus Balance 12/31/29, plus 1930 profits (excluding 1930 Dividends).....	676,032.63
Less Net Amount of 1930 profit not subject to 60% apportionment (as Exhibit -A-) attached	35,380.17*
	<hr/>
	\$640,652.46
	<hr/>

60% of above \$640,652.46 due E. J. Lord..	\$384,391.48
Plus Allowance for miscellaneous Equipment Charged to Contract Expense.....	3,500.00
Plus Allowance of 40% of Income Tax (as per Agrmt.)	20,328.50
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Portion of SURPLUS distributed to E. J. Lord	\$408,219.98
60% of CAPITAL distributed to E. J. Lord	60,000.00
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TOTAL DISTRIBUTION TO E. J. LORD (re 600 shares).....	\$468,219.98
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The \$3500 allowance is explained by Exhibit 37-D (Rec. p. 199). As testified by attorney Peters, Lord would not accept the book value of the plant and equipment because some of the articles had been entirely written off, yet really had some value (Rec. p. 58). Lord claimed \$12,000 as his 60% interest in the plant items which did not appear in the books, and on August 13, 1930, as shown by said Exhibit, the board of directors of E. J. Lord, Limited, authorized a compromise of his claim by payment to him of \$3500.

* This represents profits on contracts entered into after the option agreement, in which Lord did not share.

The \$20,328.50 figure represents a payment of \$26,904.66 for 40% of the estimated Federal taxes, less a refund of \$6,576.16 upon recomputation of the tax (Rep. p. 118, Ex. 30, 35, Rec. p. 110, 124). This sum was not paid until 1931 and held up the final consummation of the deal.

To record the transaction the bookkeeper of E. J. Lord, Limited, opened up an "E. J. Lord Settlement Account" and a "Treasury Stock Purchase Account" (Rec. pp. 107-109, Exs. 29, 30).

We submit that from the time of the first agreement between Lord and Black, and their conference with attorney Peters, the intention of the parties was clearly and logically carried out. Each step of the transaction and each distribution of profits, moreover, was approved by the board of directors of E. J. Lord, Limited, and when the deal had been completed the corporation had distributed to Lord, as shown by Exhibit 33-A-B, his original capital contribution, plus 60% of the profits and surplus of the corporation, including the \$3500 item there referred to, plus the \$20,328.50 for tax liability.

If the parties had desired simply a purchase and sale of the shares of stock they would have taken into consideration all elements that determine the *value* of stock in a going concern—the position of the corporation in the contracting business, general business conditions, the possibility of the award of lucrative contracts in the near future, etc.—and on that basis would have reached an agreement to pay a fixed sum for the stock. But this is neither what they wanted or intended. The significant thing about the entire

transaction is that there never was any attempt by the parties to reach and agree upon that value. The corporation was not making an ordinary purchase of its stock at a fixed price, as U. S. Steel might do were it to buy shares in the market to reduce its capital; what E. J. Lord, Limited, was attempting to do was to distribute to Lord his original capital contribution, plus his 60% interest in the surplus, and this is exactly what they ultimately did do, plus an equitable agreement on taxes resulting therefrom.

This was a perfectly straightforward transaction, without an attempt at either tax evasion or tax avoidance, and the intention of the parties in making the distribution in question is too clear for further argument.

But the Supreme Court seized on the fact that this agreement did not in so many words say "60% of capital plus 60% of profits" (as had been agreed by the parties), saying:

"The parties declared that it was a sale and a purchase; they declared that a part of the consideration should be a sum of money equal to sixty per cent of 'the net worth of the corporation,' *which net worth must have necessarily included capital as well as undistributed profits, and they did not, in that connection, distinguish between the two;*" (Rec. p. 33.)

This argument is not worthy of serious refutation, as even in the law things equal to the same thing are equal to each other.

The net worth of a corporation is simply the surplus of its assets over its liability. The capital of any cor-

poration, plus its accumulated surplus, is always equal to its net worth. Therefore sixty per cent of the net worth of E. J. Lord, Limited, was in fact sixty per cent of its capital plus sixty per cent of its accumulated surplus. As stated by attorney Peters, Lord was to receive "what he had originally put in the corporation by way of capital on the original organization, and that he was to also receive the undivided profits which, with the capitalization, would represent the net worth of the business" (Rec. p. 57).

The reason that the agreement was drawn as it was, rather than as the Supreme Court apparently would have demanded to recognize the essential character of the distribution, was explained by attorney Peters. According to good bookkeeping, certain plant articles had been wiped off the inventory so that if the books were taken as a standard these would not appear; however, the machinery and equipment was still in existence and still being used, and Lord wanted to have a real determination of its net worth because such machinery and equipment, though written off the books, might really have some value (Rec. p. 58).

Pursuant to that understanding the \$3500 adjustment, representing 60% of Lord's interest in items of plant and equipment which, although written off the books, had some value, was made and approved by the Board of Directors (*supra* p. 23).

The very fact that this method was followed discloses a manifest intention to divide the actual assets 60-40, rather than "sell out" on any presumed or estimated value of Lord's stock. What the parties were interested in was a distributory something that would

really be a 60% distribution of assets, and were *not* trying to value stock.

The Supreme Court also referred to the fact that part of the consideration was 60% of the net profits on incompleated contracts, saying :

“They did not say that it should be sixty per cent of the net profits but did say that it should be a sum of money equal to sixty per cent of the net profits. Was the corporation on December 13, 1929, declaring a dividend out of profits not yet earned and which might not be earned for a year longer?” (Rec. pp. 33, 34.)

Now it is common corporate practice to declare dividends at one time payable at a later time, and sometimes payments are made to stockholders of record at a future time. Similarly it is perfectly proper and legal for the board of directors of a corporation, or all of the stockholders, to agree to pay dividends in the future either upon a certain condition or upon there being a certain amount of profits then available for distribution. The only thing a corporation cannot do is to guarantee to pay dividends whether or not there is any surplus at a future time. But in the situations above discussed, and in the case at bar, it is perfectly obvious that any distribution made pursuant to a prior agreement between stockholders and the corporation, or pursuant to formal action of the board of directors, *is* a dividend.

As a matter of fact, far from this being a weak point in appellant's case, that the parties agreed that part of the consideration should be 60% of the net profits on pending contracts is one of the strongest circum-

stances sustaining the claim of appellant that this was primarily a distribution of an amount "received as dividends" rather than an ordinary sale at a fixed price. According to the practice of the corporation, profits on incompleated contracts were not computed or entered on the books even at the end of any year, but no profits were computed or set up in the books until the Government had accepted the contracts and final adjustment could be made. (Rec. p. 60.) Reference to the balance sheet of E. J. Lord, Limited, as of December 31, 1929, a photostatic copy of which was transmitted to this court but which was omitted from the printed record by stipulation of counsel, will show the very large "suspension" account which was carried for these pending contracts. Obviously, therefore, to give Lord only 60% of the book surplus as it appeared at the end of 1929 would give him less than he was entitled to. As a contractor he undoubtedly felt that he had a 60% interest in all contracts pending and in the profits thereof, and as a 60% stockholder he in fact had that right. In order to carry out the intention of the parties and give Lord his real 60% interest in the profits and surplus of the company it was necessary to do one of two things:

(1) To depart from the practice of computing profits only upon completion of the work, and estimate the status of the contracts and estimate the probable profits;

(2) To wait until the profits or losses on those contracts were established before the total amount to be paid could be ascertained.

Had there been any desire just to have the corporation "buy Lord out," or fix a price for the value of his

stock as distinguished from a bona fide attempt to prorate the capital and surplus of the company and give him his distributive share of surplus, the first course would have been chosen. The profits on the pending contracts could have been estimated as of December 31, 1929, and then discounted to arrive at the present worth of those contracts, and the corporation could then have paid Lord such a sum. But that is not what was done. Instead of that the whole consummation of the deal was deferred until the *actual* profits could be determined. The stock to be redeemed was held by the corporation as pledgee under the terms of the December 13, 1929, agreement (Ex. 9, Rec. p. 65 at 69), and the stock could not be fully paid for and the redemption finally effected until the profits on the contracts, incomplete at the end of 1929, had been determined. Obviously, from the standpoint of convenience, the method of paying for the stock in the early part of 1930 was preferable to having the matter drag on as it did, and the very fact that this cumbersome and delayed procedure was utilized shows to what extent the parties were willing to go to carry out what was essentially a sixty-forty distribution of capital and surplus.

In fact, regardless of the decision that may be reached as to the remainder of the money received by Lord, it seems impossible to hold that the sum of \$174,036.12—being his 60% of the profits on contracts pending at the close of 1929—was not received “as dividends.” If, in the ordinary course of events the corporation had agreed with Lord and Black to distribute to them, as dividends, all the profits earned on those particular contracts, and had done so, there would have been no

tax on that distribution. The only difference between that situation and the case at bar is that here, because Lord was retiring and Black keeping on, the corporation only agreed to pay Lord his share of the profits. But the mere fact that an equal distribution was not made to Black at the time cannot rob the distribution to Lord of its character as an amount received as dividends (*infra* p. 29).

There is one point referred to in the decision of the Board of Equalization, which merits brief consideration, and that is the fact that the corporation agreed to pay 40% of Lord's Federal taxes arising from the deal. How this meant that no part of the consideration paid for the stock was "received as dividends," or necessarily characterized the transaction as if it had been an ordinary sale to a third person, was not explained by the Board and was not referred to as a basis of the Supreme Court decision. The only possible significance of this provision of the agreement would be to furnish an argument that the particular sum so paid over (\$20,328.50) could not be considered as "received as dividends," because it was not paid on the understanding that it represented Lord's proportionate interest in the surplus of the corporation. Assuming that to be true, it does not vitiate appellant's entire claim for exemption any more than does the fact that \$60,000 of the consideration, representing Lord's capital contribution, prevents the balance—i. e., the part really paid as dividends—from being tax free.

If this \$20,328.50 payment is looked upon solely as an additional inducement or consideration for the transfer of Lord's stock it may be conceded that that part of the consideration was not paid or received as

dividends. This would only result in diminishing appellant's claim of exemption from \$406,569.98 to \$386,241.48.

But we submit that even this part of the consideration is exempt from taxation. There is no reason why upon redemption of stock the corporation had to give Lord exactly his 60% share of the profits, for the simple reason that by agreement between the stockholders dividends can be declared in any proportion desired (*infra* p. 29). If income taxes were to result from the distribution, and such distribution was mutually desired, it was only equity that taxes resulting therefrom should be borne in the same proportion. This particular payment meant only that Lord was getting a trifle more than his 60% interest and, since it was paid out of surplus, it should be considered as a distribution in the nature of a dividend.

In *F. G. Lamb*, 14 BTA 814 the practice of a corporation had been to pay out of surplus the Federal taxes assessed upon the corporate income distributed to the two principal stockholders. An assessment against these payments as "dividends" was sustained. There the taxpayer argued that the payments could not be dividends because they "were not formally declared in these amounts," because they "were not intended to be dividends nor were they treated as such by the stockholders or the corporation," and because the payments "were not in proportion to stock holdings" (p. 819).

But it was squarely held that since earnings or profits could be distributed without the formality of a declaration of dividends the mere fact that the div-

idends were not in proportion to the stock holdings was immaterial.

But whatever conclusion this Court reaches as to this particular item of \$20,328.50 cannot affect the question of whether the remaining moneys, over and above the return of capital, were received as dividends.

B

THAT AMOUNT WAS THEREFORE RECEIVED AS DIVIDENDS WITHIN SECTION 1391, R. L. 1925.

The normal case to which the statute in question applies is that where a going concern makes periodical disbursements to its stockholders, tagged as a "dividend." There are only two points of difference between the instant case and that typical situation :

- (1) That some of the profits here involved had been accumulating for several years ;
- (2) That there was no formal declaration of a dividend.

But these differences are differences of form, not of substance.

As to the first, it is clear that the term "dividends" includes extraordinary as well as current distributions out of surplus, *Thayer v. Burr*, 119 N. Y. S. 755 at 757 ; and as stated in *Trefry v. Putnam*, 222 Mass. 522, 116 N. E. 904 at 912 :

"The extra cash dividend was declared out of surplus earned which had accumulated during 23 years previous to March 1, 1913. Although it was

large and had been accumulating for a long time, it was not the less a cash dividend. It came to the shareholder as his individual property for the first time when declared and paid in 1916. It was not in substance or effect a distribution of capital."

It is equally clear that no formalities are required to have a dividend; the only essential is that it be a distribution of profits.

The term "dividends" is "a word of very general and indefinite meaning," has no "particular and technical signification" and is really synonymous with "distributive shares." *University v. N. C. R. R. Co.*, 76 N. C. 103, 22 Am. Rep. 671 at 672. Actually the term connotes a *division* or *distribution*. Cf. *Eyster v. Centennial Board*, 94 U. S. 500, 24 L. Ed. 188 at 189, where the court was speaking of a liquidating distribution of assets to stockholders and said:

"Such a division produces a dividend; that is to say, a part or share of the thing divided. If the division is of profits, then the dividend is of profits; if of capital, then of capital."

Usually, of course, dividends are formally declared from time to time by the Board of Directors, and distributed to all of the stockholders. But neither of these attributes is an essential of a dividend. Whenever a division of profits is made, then, regardless of formality, and regardless of whether the distribution is *called* a "dividend," it is a dividend.

Spencer v. Lowe, 198 Fed. 961, 966 (8th C.C.A.); *Smith v. Moore*, 199 Fed. 689, 692, 697 et seq. (9th C.C.A.);

Hartley v. Pioneer Ironworks, 181 N. Y. 73, 73 N. E. 576, 577;

In re Norton's Will, *supra*;

People v. Travis, 157 N. Y. S. 943, 944-945;

In re Thompson's Estate, 262 Pa. 278, 105 Atl. 273, 274.

Barnes v. Spencer & Barnes Co., 162 Mich. 509, 139 Am. St. Rep. 587, 127 N. W. 752 at 755-756, where it is said:

"A division of profits is a dividend, even though not called such and not considered such by the directors or stockholders. *Cook on Corporations*, p. 1445, and cases cited."

That is particularly true in the field of taxation where, no matter what form or device is employed, if in fact there has been a distribution of profits there has been a dividend.

Hadley v. Commissioner, 36 Fed. (2d) 543, 544 (App. D. C.) :

" it is settled law that the division of profits of a corporation among its stockholders amounts to a constructive dividend whether it is intended by the directors or stockholders to constitute a dividend or not. *Chattanooga Savings Bank C.C.A.* 17 Fed. (2d) 79; certiorari denied 274 U.S. 751, 47 Supreme Ct. 764, 71 L. Ed. 1332."

Phelps v. Commissioner, 54 Fed. (2d) 289, (7th C.C.A.), discussed *infra* p. 30.

Chattanooga Sav. Bank v. Brewer, 17 Fed. (2d) 79.

Christopher v. Burnet, 55 Fed. (2d) 527.

Nor is it necessary that the distribution be a pro-rata one, because the stockholders of a corporation can make any agreement they desire with respect to the distribution of profits, and such distributions, whether or not proportional to stock holdings, are dividends.

Joseph Goodnow & Co., 5 B.T.A. 1154 at 1158;
Breslin v. Fries-Breslin Co., 70 N.J.L. 274, 58 Atl.
 313, 318;

For applications of the foregoing principles see:

Bone v. U. S., 46 Fed. (2d) 1010:

(Excessive salaries treated as dividends though not proportionate to stock holdings.)

Duffin v. Lucas, 55 Fed. (2d) 786:

(Corporation paying debt of one shareholder.)

Frank A. Taplin, 12 B.T.A. 1264:

(“Purchase” by dominant stockholder of part of corporate assets at quarter of their value.)

In fine, a dividend is nothing but a *distribution of profits*. Before such distribution a shareholder has a certain interest in the profits of a corporation; when he gets his share of the profits, by whatever mode, he has received a dividend. As stated in *U. S. v. Phellis*, 257 U. S. 156, 66 L. Ed. 180 at 184:

“It is the appropriate function of a dividend to convert a part of a surplus thus accumulated from property of the company into property of the individual stockholders; the stockholder’s share being thereby released to and drawn by him as profits or income derived from the company.”

From the foregoing it follows—and the Supreme Court so conceded—that if the essential characteristic of the transaction in question was the distribu-

tion of profits that any profits distributed as such would be received "as dividends." And, as we have shown, all that happened in the case at bar was that Lord was surrendering his stock for his pro rata share of the capital share and profits of the corporation.

We know of no state cases dealing specifically with the problem here involved. Most of the Federal cases are inapplicable for the reason that almost every Revenue Act has made specific provision for the treatment of cases of retirement of stock or corporate dissolution. Obviously the fact that Congress chose to treat gains derived from these transactions in a certain way—either as dividends or as capital gains—sheds no light on the question now at issue.

But where, as in the 1921 act, Congress failed to provide specifically for this situation it was uniformly held that where stockholders received accumulated profits from the corporation upon retirement of their stock, or upon liquidation of the corporation, such profits so received should be taxed as "dividends" and that the capital gain sections had no application.

As stated in *Bisbee v. Midland Linseed Products Co.*, 19 F. (2d) 24 at 28:

"In order to make a sale of a capital asset, under the revenue laws in force at the time, (1921) it was necessary to sell to an outside party, or otherwise the International Revenue Department would have treated the transaction as a retirement of the shares and the proceeds as a liquidating dividend. See Internal Revenue Cumulative Bulletin, III, Vol. I, p. 47, I. T. 2034."

The case of *Phelps v. Commissioner*, 54 F. (2d) 289 (7th C.C.A.), cert. denied, 285 U. S. 558, 76 L. Ed. 946,

was decided under the Revenue Act of 1921, and it is submitted that that case should be considered as decisive of that at bar.

In that case, the facts of which are detailed more fully in the Board of Tax Appeals Report in *20 B.T.A. 866*, the W. L. Phelps Company had a common stock of 7500 shares of the par value of \$750,000, of which Northern Trust Company, Trustee, owned 2250 shares, W. L. Phelps owned 2550 shares, and Mrs. Phelps, Mrs. Voorhees and one other person each owned 900 shares. This was a family corporation. The board of directors by resolution authorized W. L. Phelps, its president, "*to purchase*" for the corporation shares of its stock *at a price not to exceed \$130 a share*. Pursuant thereto all of the stock of the corporation was purchased at \$130 a share, except 300 shares retained by Mr. Phelps, the corporation not distributing certain real property.

The Board of Tax Appeals found that the "sale of stock" was equivalent *to a surrender of stock by the stockholders for their pro rata share of the assets and surplus* and upheld the assessment of a tax on the theory that the amount of surplus received by the stockholders on surrender of their stock was received as a "dividend," within Section 201 (a) of the 1921 Act. The appeal was taken on the ground that the transaction should have been treated as a gain derived from sales of property under Section 202 of the same Act, the exact position of the Territory in the case at bar.

The Circuit Court of Appeals held, looking through the form of the transaction to its substance, *that the essence of the transaction was not a sale of stock but*

was, to the extent surplus was distributed, a distribution of profits in the nature of a dividend.

In that case the corporation had done everything possible to make the transaction look like a sale. Not a word was said about liquidation or about the payment of any pro rata share of surplus; on the contrary, the resolution passed by the board of directors spoke of a sale and purchase of stock, and that at a price not to exceed a certain sum. But this, as the Board of Tax Appeals said, was in legal effect "*to all intents and purposes an agreement among the stockholders to surrender their stock in exchange for a pro rata share of the distributable surplus*" (20 B.T. A. at 873), and, as stated by the Seventh Circuit (p. 291) :

"If, under the facts stated, we are bound by the plain meaning of the language employed in the resolution referred to in the statement of facts, then of course the transactions in controversy should be considered as sales, for that is what the resolution termed them, and pursuant thereto there was an exchange of stock for money. But in all relations of life it oftentimes happens that the thing done speaks so audibly that equity is prevented from hearing the language of the parties, and will classify the act by its real name rather than by the name which the interested parties have given it. In such instances the substance of the transaction will control the form, and the Board therefore was warranted in considering both form and substance in arriving at its conclusion. *United States v. Phellis*, 257 U. S. 156, 42 S. Ct. 63, 66 L. Ed. 180; *United States v. Klausner* (C.C.A.) 25 F. (2d) 608."

Now in the Phelps case there was a studied purpose on the part of the corporation and the stockholders to

get within the capital gain sections and every act that they did in making the distribution was directed toward that end. In the case at bar, however, there was no such attempt to color the transaction in any way; the parties simply clearly and logically carried out their intention to distribute to Lord his share of the surplus. Yet the Supreme Court, because neither the minutes of the board of directors meeting of December 7, 1929, nor the agreement of December 13, 1929, nor any of the formal records of the corporation, referred specifically to the word "dividend," refused to look at the substance of the transaction and considered it as an ordinary sale!

If in the *Phelps* case the retirement of stock amounted to an agreement of the shareholders "to surrender their stock in exchange for a pro-rata share of the distributable surplus," *a fortiori* that is true in the case at bar.

And if in the *Phelps* case a "dividend" had been received, *a fortiori* an amount had been "received as dividends" in the case at bar.

It may be urged that the Phelps case is not an authority for appellant because the Revenue Act of 1921 had a definition of the word "dividend":

"Sec. 201. (a) That the term 'dividend' when used in this title means any distribution made by a corporation to its shareholders or members, whether in cash or in other property, out of its earnings or profits accumulated since February 28, 1913, except a distribution made by a personal service corporation out of earnings or profits accumulated since December 31, 1917, and prior to January 1, 1922."

But this does not subtract anything from the force of that decision. As we have shown, a “dividend” *means* any distribution out of earnings or profits regardless of the manner or form in which it is made, and the only effect of the statutory definition was to prevent dividends being taxed which were declared out of earnings and profits accumulated prior to February 28, 1913—the effective date of the Income Tax Act.

Tax Assessor Hill felt that the distribution in question could not have been received “as dividends” because Black did not receive any equal distribution (Rec. p. 14 at 18), and this seemed to be the main basis of the Board’s decision (see Rec. p. 14 at 18).

As pointed out above, however, dividends need not be pro-rata, for stockholders can make any agreement they please about distributing surplus. (Supra p. 29.) If the corporation was trying to pay Lord his share of profits that amount was tax-free whether or not it at the same time gave Black his share. The Supreme Court admitted that if Black had received his pro-rata share that would have been tax-free, though he should immediately re-invest it all in the company (Rec. p. 34). How that would affect the essential character of the transaction between Lord and the corporation, however, is not explained.

In point of fact Black did receive just as much as Lord in the transaction. When Lord was eliminated from the company, Black became the actual, if not the technical, owner of all of the assets of the corporation. The same situation existed and the same contention was made in the Phelps case. There the taxpayer contended that the word “div-

idend" or "distribution" had to be "without reference to any surrender of stock," and since Phelps retained 300 shares, the other distribution could not be a "dividend" or "distribution" because "distributions must be made ratably to all stockholders" (20 B.T.A. at 873). The Board of Tax Appeals, answering these contentions, pointed out that the test of a distribution was not whether or not a stockholder surrendered his stock, nor was it necessary that dividends be pro-rata to stock holdings, and the fact that Phelps retained some stock was immaterial as "... the 300 shares retained by the president represented only the value of the undistributable property, and *when all other stockholders were eliminated he was left with 300 shares of stock as the sole owner of the corporation and virtual owner of all that remaining property*" (20 B.T.A. 873).

Similarly the Seventh Circuit pointed out that the transaction in question was not primarily a "sale," but the "sale" was only incident to the transaction and, answering the other objection of the taxpayer, said:

"... The fact that Mr. Phelps received money for part of his stock and retained the remaining outstanding stock cannot militate against such conclusion. *He was thereby, in effect, the owner of the undisposed of assets of the corporation, which consisted only of the Jefferson street property.* Technically, as between the stockholders and the corporation, it was not a complete liquidation in the sense that all the assets had been converted into cash and distributed; *but as between the stockholders themselves, for all practical purposes, there was in effect a complete distribution,*

which was evidently made by agreement of the parties and one which they were fully authorized to make. Breslin v. Fries-Breslin Co., 70 N. J. Law, 274, 58-8, 313; Joseph Goodnow & Co. v. Commissioner, 5 B.T.A. 1154; F. G. Lamb v. Commissioner, 14 B.T.A. 814." (54 Fed. (2d) at 292-293.)

That this statement can be accurately applied to the case at bar cannot be doubted.

In its essence the case at bar is indistinguishable from the case of *Commissioner v. Ward*, 65 Fed. (2d) 758 (3rd C.C.A.). There a party withdrew from a building and loan association. The by-laws of the association provided that upon such a withdrawal stockholders should be entitled to their proportionate share of the earnings and surplus of the corporation, and that is what the shareholder in fact received. The transaction therefore was treated as if the shareholder had received a dividend and was not treated as a capital gain, the Court saying, at page 759:

"We think the profits made and apportioned among the stockholders constituted a dividend of profits. This is so, although the profits were accumulating until the shares matured instead of being declared and paid at regular intervals. See *Cary v. Savings Union*, 22 Wall. 38, 22 L. Ed. 779."

In the case at bar there is of course no charter or by-law provision corresponding to that of the building and loan association in the *Ward* case. But a pro-rata share of surplus is what a shareholder of a corporation is entitled to receive upon dissolution of the corporation, or upon his withdrawal therefrom, and in point of fact that is exactly what was intended to be given, and was given, to Lord upon his retirement.

We submit, therefore, that the Supreme Court erred in failing to consider the *substance* of the transaction here involved, and that upon a consideration thereof by this court appellant's claim for exemption should be allowed.

II.

THE COURT ERRED IN HOLDING THE DIFFERENCE BETWEEN THE COST OF APPELLANT'S STOCK AND THE AMOUNT HE RECEIVED THEREFOR WAS TAXABLE.

(Assignment of Error No. 3)

This argument is advanced only if appellant's claim for exemption is denied and the transaction treated as an ordinary sale of stock.

In these days of heavy income taxes it is a commonplace for persons to pay, under the Federal capital gains sections, a tax on the profits derived from the sale of stock, and the profit is measured by the difference between the cost of the stock and the price for which it is sold. This is true, although the stock may have been bought, say in 1926, and sold in 1934. We are prone to assume, therefore, that all taxing systems tax such profits in the same manner, and are liable to lose sight of the fact that unless specific provision is made therefor, no such result normally follows from the sale of stock purchased several years back.

To illustrate: If a man buys stock in 1900 for \$50.00, that stock may steadily increase in value until, say in 1913, it is worth \$250.00. If at the end of 1913 that stock is sold for \$300.00, it is obvious that he has not made a gain *during the year 1913* of \$250.00. If he has gained any income at all it would be only \$50.00; that

is, he has not gained *during the year 1930* the difference between what he bought the stock for in 1900 and sold it for in 1913, but only the difference between what the stock was worth at the beginning of the taxation period and what he sold it for at the end.

It is submitted, therefore, that the Court erred in holding that in this case a tax could be assessed on the difference between the cost to Mr. Lord in 1926 of his stock, and the amount which he received therefor in 1930.

Unquestionably we are here in the realm of "local statutory instruction" of tax laws. Ordinarily this Court would not upset a decision by the Territorial Supreme Court on such a matter unless manifestly erroneous. In this case, however, the Supreme Court overruled, *sub silentio*, one of its own decisions rendered in 1906, which in turn was based upon a United States Supreme Court decision. Consequently the correctness of the ruling now made should be examined.

In *Castle v. Tax Assessor*, 18 H. 129, one J. B. Castle bought stock in 1898 and sold it in the latter half of 1905 at a profit of \$120,000. The taxation period covered the six months prior to January 1, 1906, and it was sought to levy a tax on the \$120,000 profit because the stock had been sold during that period. Castle contended, however, that the profit was not taxable because it was not an income "derived during the taxation period in question, namely, from July 1, 1905, to January 1, 1906."

This contention was sustained, the Supreme Court of the Territory saying:

" All that the statute attempts to tax is the income derived during a certain period. The

period in question in this case was for the six months prior to January 1, 1906. R. L., Sec. 1278, as amended by Act 87 of the Laws of 1905, provides for a tax on the amount derived 'during the taxation periods as herein defined,' and that the first taxation period 'shall be the half year immediately preceding the first day in January, 1906.' R. L., Sec. 1280, as amended by the same act, provides that in estimating gains, profits and income they shall be derived 'during said taxation period.' The income in question was not derived during the six months preceding January 1, 1906, and therefore was not taxable as gains, profits and income derived during that period. See *Gray v. Darlington*, 15 Wall. 63."

The facts in that case are indistinguishable from those in the case at bar. Similarly the statute then in question is practically identical with the statute under which the present tax was assessed. Section 1278, R. L. 1905, like its successor, Section 1388, R. L. 1925, provided for an *annual* levy on "gains, profits and income" derived (in the first statute) or received (in the second) *during the taxation period*. And Section 1280, R. L. 1905, providing what "income" included, has been carried over into Section 1390, R. L. 1925, *in haec verba* (though the end of Section 1390 now contains an additional proviso which has no bearing on the question now presented).

The *Castle* case, and the United States Supreme Court case upon which it was based, were urged as authority for the taxpayer's contention in the case at bar, but the Supreme Court, repudiating its earlier decision in the *Castle* case, refused to follow the *Darlington* case.

In *Gray v. Darlington*, 15 Wallace, 63, 21 L. Ed. 45, the taxpayer had purchased certain bonds in 1865. In 1869 he sold the bonds at a profit of \$20,000, and it was sought to levy a tax against this profit for the year 1869. The Court squarely held that the mere fact that the property had appreciated in value between 1867 and 1869, and that the entire profit was first realized in 1869, did not make that profit a "gain, profit or income" for the year 1869, and that that profit of \$20,000 was not taxable. In the course of its opinion, the Court said:

"The question presented is whether the advance in the value of the bonds, during this period of four years, over their cost, realized by their sale, was subject to taxation as gains, profits, or income of the plaintiff for the year in which the bonds were sold. The answer which should be given to this question does not, in our judgment, admit of any doubt. *The advance in the value of property during a series of years can in no just sense be considered the gains, profits or income of any one particular year of the series, although the entire amount of the advance be at one time turned into money by a sale of the property.*" (21 L. Ed. at 46.)

That case was decided under an act of Congress of March 2, 1867, which provided in part:

"There shall be levied, collected, and paid *annually* upon the gains, profits, and income of every person whether *derived* from any kind of property, rents, interest, dividends, or salaries, or from any profession, trade, employment, or vocation, or *from any other source whatever*, a tax of five per centum on the amount so *derived* over \$1000 And the tax herein provided for shall be assessed, collected, and paid

upon the gains, profits, and income *for the year ending the 31st of December next preceding the time for levying, collecting, and paying said tax.*"

The above section is practically identical with Section 1388, R. L. 1925, which provides :

Sec. 1388. *Rate on Person's Income.* There shall be levied, assessed, collected and paid annually upon the gains, profits and income received by every individual residing in the Territory, from all property owned, and every business, trade, profession, employment or vocation carried on in the Territory a tax in accordance with the following schedule on the amount so received *during the taxation period as herein defined:*

Another part of the above quoted section of the Congressional act provided :

"In estimating the gains, profits, and income of any person, there shall be included all income derived from interest upon notes, bonds, and other securities of the United States, *profits realized within the year* from sales of real estate purchased within the year, or within two years previous to the year for which income is estimated, *and all other gains, profits, and income derived from any source whatever.*"

This is the counterpart of Section 1390, R. L. 1925, as amended by Act 133, S. L. 1927, the relevant portion of which provides :

"Section 1390. *Income Includes What.* In estimating the gains, profits and income of any person or corporation, there shall be included all income derived from interest upon notes, bonds and other securities, ; profits realized within the taxation period from sales of real estate,

..... ; ; the amount of sales of all movable property, less the amount expended in the produce or production of the same, and in case of a person not including any part thereof consumed directly by him or his family; money and the value of all personal property acquired by gift or inheritance, and *all other gains, profits and income derived from any source whatsoever during said taxation period*”

The whole point of the *Darlington* case is that the advance in the value of personal property over a period of years cannot be considered as a “gain, profit or income” for the particular year in which the sale was made and the gain realized. As stated by the Court:

“Mere advance in value in no sense constitutes the gains, profits or income specified by the statute. It constitutes and can be treated merely as increase of capital.”

In reaching its conclusion in the instant case, the Supreme Court sought to bulwark its conclusion by reference to Section 1390, dealing with the sales of movable property, the court said:

“The requirement of the statute was that in January, 1931, liability would accrue for taxes on income which was ‘received’ or ‘derived’ during the taxation period, which was the year 1930; and this is made even more clear with reference to the sales of movable property when the statute declares that in estimating the profits ‘there shall be included the amount of less the amount expended in the purchase’. The legislature did not, in this connection, make any exception of those parts of the gain in value which did not ac-

crue during the taxation year and the court cannot now make the exception."

(Record pp. 35-36.)

There are several reasons, however, why the section partially quoted from above has no application.

In the first place that portion of Section 1390, R. L. 1925, as amended by Act 133, S. L. 1927, refers only to the sale of *movable* property. While the expression "movable property" may be held to refer to all property which is not real estate, the more usual use of the phrase is to denote *tangible* property rather than intangible property such as shares of stock which do not properly belong in the category of either movables or immovables. The reference in Section 1390 to the consumption of such property shows that only tangible property was meant to be covered by the phrase in question.

In the second place, the Supreme Court itself has held in *Frear v. Wilder*, 25 H. 603, that Section 1390, R. L. 1925, in which the "movable property" phrase appears, does not itself purport to levy any tax or prescribe what is or is not included in the term "gains, profits or income." The only section which does that is Section 1388. Consequently, therefore, if the principle of the *Darlington* case is applied—that the gradual increase in value is not in fact "gain, profit or income" derived or received during the year in which the sale is made, the fact that provisions for treating such a transaction were made in Section 1390 would be immaterial. We refer the Court to the *Frear* case above cited where the exact point was raised and determined.

But the Territorial Supreme Court says that the *Darlington* case has been distinguished, citing *Hayes v. Gauley Mt. Coal Co.*, 247 U. S. 189, at 191-193; 62 L. Ed. 1061, at 1063 (Record p. 36). The *Hayes* case did not purport to weaken the force of the *Darlington* decision, but simply held that the act then under consideration was so differently worded from the act considered in the *Darlington* case that the latter decision was not controlling.

That the *Darlington* case is still the law appears from the fact that in a case subsequent to the *Hayes* case, to-wit: *Lynch v. Turrish*, 247 U. S. 219 at 230; 62 L. Ed. 1087 at 1093, the Court said, speaking of the *Darlington* case, "This case has not been since questioned or modified."

It was sought in the *Lynch* case to distinguish the *Darlington* case on the ground that the act of 1913 made the income tax one on income "arising or accruing" in the preceding calendar year while the act of 1867 made the income tax one on income "derived," but, as the Court said, while there might be a shade of difference between the words "it cannot be granted that Congress made that shade a criterion of intention and committed the construction of its legislation to the dispute of purists."

Then follows this language:

"Besides, the contention of the government does not reach the principle of *Gray* and *Darlington*, which is that the gradual advance in the value of property during a series of years in no just sense can be ascribed to a particular year, not therefore as "arising or accruing," to meet the challenge of

the words, in the last one of the years, as the government contends, and taxable as income for that year or when turned into cash. *Indeed, the case decides that such advance in value is not income at all, but merely increase of capital, and not subject to tax as income.*"

This is exactly the point in the case at bar—that not only should the tax, if any, be based only on the difference between the value of the stock on January 1, 1930, and the amount received therefor, but that in point of fact the gain derived by Mr. Lord was not profit at all but was increase in capital.

There are likewise several striking analogies between the Congressional act under which the *Darlington* case was decided, and the territorial act now in question. Section 1390, as amended, by Act 133, S. L. 1927, provides for profits "realized" within the taxation period from sales of real estate, and provides the exact method of determining the gain where the property is sold either less or more than five years before the sale. So, in the *Darlington* case a similar provision was made for the determination of gains upon the sales of real property. Both statutes contain a general provision requiring all gains, profits and income derived from any source whatever, in addition to the sources enumerated, to be included in the estimate of the assessor. The language of the *Darlington* case is precisely applicable to the case at bar:

" and except, however, in this and similar cases, and in cases of sales of real property, the statute only applies to such gains, profits and income as are strictly acquisitions made during the year preceding that in which the assessment is levied and collected." (21 L. Ed. at 46.)

Consequently, it is submitted, the Supreme Court of the Territory erred in overruling the *Castle* case, and in failing to follow the *Darlington* case.

We may also mention one certain error in the computation of the tax. The tax is on income derived or received *in 1930*. But the evidence is that the payment of 40% of Lord's Federal taxes—being \$20,328.50—was not made until *1931*; (Ex. 29, Rec. p. 108; Ex. 30, Rec. p. 109; Rec. p. 118), hence clearly no tax for the year 1930 was payable on that amount on any theory.

CONCLUSION

So far as appellant's claim for exemption is concerned there is only one question to be determined—should or should not the *substance* of the transaction control the form, and the manifest intention of the parties prevail over their failure to actually mention the word "dividend" in the formal documents? If it should, then clearly the distribution in question is tax-free, as within the letter, spirit and intent of the act in question.

In any event, we submit that it was clear error to tax the gradual gain in value of appellant's stock as a profit for the year 1930.

Respectfully submitted this 10th day of February, 1935.

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IN THE
United States Circuit Court of Appeals
FOR THE
NINTH CIRCUIT

EDMUND J. LORD,

Appellant,

vs.

TERRITORY OF HAWAII,

Appellee.

UPON APPEAL FROM THE SUPREME COURT
OF THE TERRITORY OF HAWAII

BRIEF FOR APPELLEE

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No. 7543

IN THE

United States Circuit Court of Appeals

FOR THE

NINTH CIRCUIT

EDMUND J. LORD,

Appellant,

vs.

TERRITORY OF HAWAII,

Appellee.

BRIEF FOR APPELLEE

I.

STATEMENT OF FACTS

In the year 1931 the appellant filed in the First Taxation Division of the Territory of Hawaii, an income tax return for the twelve months preceding January 1, 1931. The return showed, amongst other income, income in the amount of \$408,219.98 received from E. J. Lord, Limited, a corporation, which income appellant claimed to be exempt from taxation for the alleged reason that it was dividends received from a corporation which was subject to and had paid a territorial income tax (Record, pages 1 to 7). Thereafter the income tax assessor notified the appellant that the return was not in conformity to law and assessed the appellant upon net taxable income in the

amount of \$398,224.40 (the amount of the aforesaid income claimed to be exempt together with other income less certain deductions and exemptions) a territorial income tax in the amount of \$18,686.22 (Record, pages 8 to 11).

From this assessment the appellant appealed to the Territorial Board of Equalization (Record, pages 11 to 13). Upon the hearing of the appeal, both the appellant and the Territory of Hawaii adduced evidence (Record, pages 38 to 278). The Territorial Board of Equalization sustained the contentions of the Territory and, after finding particular facts (Record, pages 14 to 17), made findings that the amount of \$408,219.98 was not intended as or received by the appellant as dividends, but, to the contrary, that the said amount was taxable income derived from the sale of stock by the appellant to E. J. Lord, Limited, the corporation. Upon all of the evidence the Territorial Board of Equalization concluded that "this Board finds for the tax assessor and hereby decides that the taxpayer had for the twelve months preceding January 1, 1931, a taxable income of \$398,224.40 on which a territorial income tax amounting to \$18,686.22 shall be paid" (Record, pages 18 and 19).

Thereafter the appellant appealed from the decision of the Territorial Board of Equalization to the Supreme Court of Hawaii (Record, pages 19 to 21). The Supreme Court of Hawaii rendered its decision (32 Hawaii, 896), which, after carefully reviewing the evidence and the contentions of the parties, found that the amount received

by the appellant was not received as a dividend. It found that the transaction, out of which the said sum was received, was a sale by the appellant to E. J. Lord, Limited, of 600 shares of the latter's stock. It decided that the amount received was taxable income.

The Supreme Court affirmed the decision of the Territorial Board of Equalization. A judgment was thereafter entered in conformity to the decision (Record, pages 37 and 38). From this decision and judgment the appellant appealed to this Honorable Court.

The material facts are stated in the said decision of the Supreme Court (Record, pages 24 to 31). We adopt the statement of facts made by the Supreme Court. The Supreme Court said:

"E. J. Lord and E. E. Black, having been prior thereto associated in the contracting and building business, in September, 1926, formed a corporation under the name of E. J. Lord, Limited. The corporation had a capital stock of \$100,000 in one thousand shares, six hundred shares of which were issued to E. J. Lord and four hundred shares to E. E. Black, Lord contributing in payment of the stock money or other capital of the value of \$60,000 and Black contributing money or other capital of the value of \$40,000. Apparently to comply with the requirements of the law relating to the formation of corporations, three other stockholders were named, each as the holder of one share, but, as testified to by Black at the trial before the board, these three held the shares only 'nominally' and were in reality 'dummies.' In each of the annual reports subsequently filed with the treasurer of the Territory only two persons were named as holders of the capital stock and these

were E. J. Lord as holding six hundred shares and E. E. Black as holding four hundred shares.

The corporation met with a large measure of success and received substantial profits from its operations.

Late in 1929 E. E. Black, whose ambition had long been to form and control a corporation of his own, and E. J. Lord, who, because of ill health and perhaps for other reasons, desired to retire from the active pursuit of that business, after various discussions came to the understanding that Lord would retire and that Black would continue the business. On December 13 of that year they signed a written document which had been prepared by learned counsel, a former chief justice of this court, stating the terms of the understanding which the two had so reached. There was included in the agreement the grant to E. J. Lord Company, Limited, of an option to acquire the six hundred shares owned by E. J. Lord, for a consideration therein stated. Shortly thereafter the option was accepted by the corporation and in due course, in part early in 1930 and in part in December of 1930, the sum of \$468,219.98 was paid to Lord in accordance with the terms of the contract.

Subsequent to the acceptance of the option the name of the corporation was changed to E. E. Black, Limited, and its capital stock was reduced to \$40,000 divided into four hundred shares, all of which was held by E. E. Black. * * *

The main question is, what was the nature of the transaction between the corporation and Lord? As to the \$60,000 there is no dispute. It was a restoration to Lord of the capital which he had contributed. As to the remainder, was it received by Lord as a dividend? The board of directors of E. J. Lord, Limited, held a meeting on December 7, 1929, to consider the proposal then pending. Under the title of 'Purchase of Stock' the minutes of that meeting say: 'Mr. E. E. Black moved that as Mr. E. J. Lord was willing to

sell all his stock of E. J. Lord, Ltd., the company was to redeem the 600 shares for which the company was to pay for the said shares in the following manner: (1) The sum of money equal to 60% of the net worth of the company as of December 31st, 1929; (2) the sum of money equal to 60% of the net profits of all contracts awarded and not completed on December 31, 1929; (3) the sum of money equal to 40% of the amount to which Mr. E. J. Lord may become liable for federal and territorial income taxes upon income accrued and to accrue to him resulting from the sale of said 600 shares. Mr. Lord agreed to give the company an option to purchase the above mentioned stock to February 28th, 1930, and to have an agreement drawn signed by both parties covering the above option, price and payments to be made, a copy of such agreement to be entered into the minute book.' This motion carried unanimously. Another motion adopted at the same meeting was: 'That the company upon the exercise of the option cause its articles of association to be amended' so as to effectuate a change of name.

Then followed the carefully drawn agreement of December 13, 1929, which was intended, as appears from the evidence, to be a written record of what the agreements were. Omitting irrelevant portions, that instrument recited and declared, referring to E. J. Lord's six hundred shares of capital stock, that the corporation 'desires to redeem said shares of stock'; that Lord 'is willing to accept as consideration for the sale of said stock' to the corporation and the corporation 'is willing to pay' to Lord 'for the redemption of said stock, a sum of money equal to sixty per cent (60%) of the net worth' of the corporation 'as of December 31, 1929, and a sum of money equal to sixty per cent (60%) of the net profits yet to accrue' to the corporation 'by its completion of the respective works contemplated by certain executory contracts to which' the corporation 'is a party, remaining uncom-

pleted, and the further sum of money equal to forty per cent (40%) of the amount to which' Lord 'may become liable to the United States of America and/or the Territory of Hawaii for income taxes upon income accrued and/or to accrue to him by reason of and resulting from the exercise' by the operation 'of the option hereby granted and the consummation of the sale of said six hundred (600) shares of the capital stock' of the corporation; that 'the net worth of the' corporation 'cannot be determined until the books' of the corporation 'have been closed for the year 1929 and an audit made thereof;' that certain enumerated contracts were uncompleted; that therefore Lord 'does hereby * * *' (a) 'give and grant' to the corporation 'an option, irrevocable within the time for acceptance herein limited, to purchase free from encumbrances the said six hundred (600) shares of the capital stock' of the corporation 'so owned by him * * * for the consideration hereinafter set forth,' (b) 'assign and deliver' to the corporation the same six hundred shares, duly endorsed, 'by way of pledge to secure the performance' of Lord's covenants and (c) appoint the corporation his attorney 'upon the exercise of the option hereby granted' to cause the said six hundred shares 'of the capital stock * * * to be redeemed' by the corporation and 'to be recorded on the proper books' of the corporation. The corporation, on the other hand, agreed (1) to close its books as of December 31, 1929, and to have them audited, (2) to faithfully complete the uncompleted contracts in as economical manner as possible, (3) to have its books open to the inspection of Lord at all times and (4) that 'upon the exercise of the option by it to it hereby granted,' it will 'as soon as may be, cause its articles of association to be amended' so as to effectuate the desired change of name. Both parties mutually covenanted and agreed therein (1) that 'the option hereby given shall be open for acceptance up to, but not after the 28th day of February, 1930,'

(2) that 'the purchase price of the said stock' should be, reciting the precise language earlier in the document used, 'a sum of money equal to sixty per cent (60%) of the net worth' of the corporation as of December 31, 1929, 'a sum of money equal to sixty per cent (60%) of the net profits yet to accrue' to the corporation 'by its completion' of the uncompleted contracts and 'the further sum of money equal to forty per cent (40%) of the amount' which Lord 'may become liable' to pay 'for income taxes upon income accrued and to accrue to him by reason of and resulting from the exercise' by the corporation 'of the option hereby granted and the consummation of the sale' of the six hundred shares. The document further recites 'that such purchase price shall be paid' to Lord as follows: 'The sum of money equal to sixty per cent (60%) of the net worth' of the corporation 'as of December 31, 1929, forthwith upon the exercise' by the corporation 'of the option hereby granted to it. In the event that the amount so payable exceeds the sum of two hundred fifty thousand dollars (\$250,000.00), the amount of the excess over that sum may be retained' by the corporation 'until and paid by it to' Lord 'upon the completion of the St. Louis Heights contract and the receipt by it of the full consideration for the performance thereof, the sum of money equal to sixty per cent (60%) of the net profits yet to accrue from each of the foregoing enumerated uncompleted contracts when completed and the moneys, bonds or other consideration accrued and payable or deliverable' to the corporation 'thereunder, reduced to possession, and the sum of money equal to forty per cent (40%) of the income tax' which Lord might become liable to pay 'for income taxes upon income accrued or to accrue to him by reason of and resulting from the exercise by' the corporation 'of the option hereby granted and the consummation of the sale' of the six hundred shares 'forthwith upon assessment.'

Under date of February 15, 1930, Lord signed a paper whereby he acknowledged receipt of the sum of \$250,000 in money or its equivalent, from the corporation, which paper read as follows: 'E. J. Lord, Limited, having duly accepted the option granted by me to it by the indenture of agreement between us dated December 13, 1929, and the sum of two hundred seventy-three thousand eight hundred fifty-five dollars and thirty-six cents (\$273,855.36) having been found to be sixty (60%) of the net worth of E. J. Lord, Limited, as of December 31, 1929; I hereby accept in lieu of cash and acknowledge receipt from E. J. Lord, Limited, in payment of the sum of two hundred fifty thousand dollars (\$250,000.00) on account of the purchase price of the six hundred (600) shares of the capital stock of E. J. Lord, Limited, the subject of said indenture, the following enumerated notes, bonds and cash,'—followed by an enumeration of the property transferred and received."

II.

APPELLANT'S "ANALYSIS OF THE CASE"

The decision of the Supreme Court is a complete answer to every contention and argument made by the appellant. The Supreme Court carefully considered all of the evidence. Its decision is in accord with the findings made by the Territorial Board of Equalization. Those findings are supported by abundant evidence throughout. It correctly construed the territorial income tax statute (Chapter 103, Revised Laws of Hawaii 1925). Its construction is in accord with the construction given the statute by the administrative officers (Record, pages

233 to 241, 260, 261). It then applied the law to the facts and arrived at the inevitable result that the assessment should be sustained and the decision of the Territorial Board of Equalization affirmed. The decision is sound in every respect, and its language and meaning too clear to admit of any argument.

The appellant has failed to show wherein the Supreme Court erred in any particular. He does not argue that there was an absence of evidence or insufficient evidence to support the findings made in the decisions he has appealed from. His entire argument is directed to the points, first, that the administrative officials, and then the Territorial Board of Equalization, and then the Supreme Court erroneously construed a local territorial income tax law, and, second, that the findings of fact should have been made in conformity to his interpretation of the evidence. He desires this court to construe a local territorial tax statute differently than the highest court of the Territory has construed it. He wants this court to make findings of fact contrary to those of the Territorial Board of Equalization and the Supreme Court.

It should be observed that the appellant's two contentions, namely, that the amount (\$408,219.98), received by the appellant from E. J. Lord, Limited, was received by him as a "dividend," (appellant's brief, pages 11 to 37), and, that even though the moneys were not received by appellant as a "dividend" still no tax was assessable thereon because the increase in value of the shares sold accrued during the years 1926 to 1930, both years inclusive (ap-

pellant's brief, pages 37 to 46), were made before the Supreme Court (Record, pages 26 and 27). The Supreme Court fully considered both contentions and fully disposed of them (Record, pages 31 to 37).

The only contention not made before the Supreme Court is that contained in the last paragraph of appellant's brief, immediately before its "conclusion." This contention was not advanced before the Territorial Board of Equalization nor the Supreme Court. It is not covered or raised by the assignment of errors.

Beside the points, hereinafter made, as to the issues before this Honorable Court upon an appeal from the Supreme Court, the principal question in the case at bar is whether the transaction between Lord and the corporation, E. J. Lord, Limited, was a sale of stock by Lord to the corporation, from which sale he derived the income assessed by the Territory, or whether the corporation paid out, and Lord received a dividend. That issue is clearly set forth in the decision of the Supreme Court. The Supreme Court did not answer that question from the form of the transaction alone, as stated by the appellant on pages 9 and 10 of his brief, but it considered all of the evidence. It reviewed the evidence and considered the evidence of Black (Record, pages 24 and 25), the minutes of the corporation (Record, pages 27 and 29), the written agreement (Record, pages 28 to 31), the payments made to and the receipts given by Lord and all of the testimony (Record, page 32). The court said at page 32, "* * * The essence of the transaction, as disclosed by

the minutes of the corporation, by the formal memorandum of contract, by the formal receipt *and by the testimony*† is that Lord sold to the corporation * * * the six hundred shares of stock * * *." After considering all of the evidence it decided that the formal agreement of sale correctly set forth the nature of the transaction and the intention of the parties.

III.

CONTENTIONS OF THE APPELLEE

The appellee, the Territory of Hawaii, respectfully contends:

1.

That the decision of the Supreme Court of Hawaii involves and is based upon the construction of a local statute, and, that the Honorable, the United States Circuit Court of Appeals, should not disturb such a decision.

2.

That the decision of the Supreme Court of Hawaii involves issues and findings of fact, which findings are supported by substantial evidence, and that the Honorable, the United States Circuit Court of Appeals should not, under such circumstances, disturb the same.

3.

That the amount received by the appellant from the corporation, E. J. Lord, Limited, in consideration of his

† (*Italics supplied unless indicated otherwise.*)

selling to the said corporation 600 shares of stock, was not a "dividend" within the meaning of that term as it is used in Section 1391 of the Revised Laws of Hawaii, 1925.

4.

That the amount received by the appellant from the corporation, E. J. Lord, Limited, was taxable income derived from the sale of 600 shares of stock.

5.

That the exemption claimed by the appellant should not be construed in his favor, but should be strictly construed in favor of the government.

6.

That the court did not err in holding that the difference between the cost of appellant's stock and the amount he received therefor was taxable.

7.

That the tax upon the income of the appellant for the year 1930 was correctly computed.

8.

That the appellant has waived any objection to the computation of the tax.

9.

That the assignments of error do not raise for review the question as to whether the tax was correctly computed.

IV.

ARGUMENT.

1.

THAT THE DECISION OF THE SUPREME COURT OF HAWAII INVOLVES AND IS BASED UPON THE CONSTRUCTION OF A LOCAL STATUTE, AND, THAT THE HONORABLE, THE UNITED STATES CIRCUIT COURT OF APPEALS, SHOULD NOT DISTURB SUCH A DECISION.

It not only appears from the entire record, and particularly from the decision of the Supreme Court of Hawaii (Record, pages 25, 26, 34, 35 and 36), but it also appears from appellant's argument that a construction of Chapter 103, Revised Laws of Hawaii, 1925, the Territorial income tax statute is involved. The Supreme Court of Hawaii said in its decision: "Subsequent to the acceptance of the option the name of the corporation was changed to E. E. Black, Limited, and its capital stock was reduced to \$40,000 divided into four hundred shares, all of which was held by E. E. Black. Section 1391, R. L. 1925, which is part of chapter 103, relating to income taxes, provides that 'in assessing the income of any person or corporation there shall not be included the amount received from any corporation as dividends upon the stock of such corporation if the tax of two per centum has

been assessed upon the net profits of such corporation as required by this chapter.' It is undisputed that the money paid to E. J. Lord under the contract referred to, other than the sum of \$60,000 which came from capital, was actually paid by the corporation out of undivided profits, partly earned prior to the date of the contract and partly earned after the date of the contract and that upon all of these undivided profits the corporation had paid the tax of two per cent required by law. The contention of the taxpayer-appellant is that the moneys received by him in 1930 (other than \$60,000 thereof) were received by him 'as a dividend' out of profits which had already borne the statutory tax of two per cent and are, therefore, exempt from taxes as income of E. J. Lord. The contention of the Territory, on the other hand, is that in the transaction between Lord and Black there was not any payment of a dividend and that there was simply a sale by Lord and a purchase by the corporation of the six hundred shares of the capital stock owned by Lord and a payment therefor of the purchase price in which was not involved or included any idea of a dividend. A second claim by the appellant is that even if the moneys in question were not received by Lord 'as a dividend' but are to be deemed gains or profits derived from the sale of personal property, still no tax is assessable thereon because the increase in value of the six hundred shares over and above \$60,000 accrued during the years 1926, 1927, 1928 and 1929 and did not accrue wholly during the taxation year of 1929." (Record, pages 25 and 26.)

The court was called upon to determine whether the words of the statute "the amount received from any corporation as dividends upon the stock of such corporation" included the amount received by the appellant (other than \$60,000 thereof) from the corporation, E. J. Lord, Limited, upon the sale of his stock. The appellant contended that it was included, and the Territory maintained that it was not included. Hence, a question of statutory construction is involved.

The following language clearly shows that the Supreme Court of Hawaii was faced with the construction of a Hawaiian statute:

"Another consideration, not controlling and yet relevant, is that the exemption provided for in the provisions of section 1391, above quoted, is that in favor of amounts received from a corporation 'as dividends upon the stock' of that corporation. This would seem to presuppose the payment of a dividend to one who holds stock rather than to one who by the very transaction is relinquishing the stock to the corporation. If the legal possibility of one who is relinquishing stock in the same transaction receiving a dividend upon that stock is not excluded, at least it would require some evidence on the part of the parties to the transaction to indicate that some or all of the moneys paid to the outgoing stockholder were being paid as a dividend. There are no such indications in the case at bar." (Record, page 34.)

The second contention made by the appellant also involves the construction of the same statute. This clearly appears from the decision of the Supreme Court of Hawaii. It said: "The other contention of appellant likewise

cannot be sustained. Section 1388, R. L. 1925, provides that 'there shall be levied, assessed, collected and paid annually upon the gains, profits and income received by every individual residing in the Territory, from all property owned, * * * a tax in accordance with the following schedule on the amount so received during the taxation period.' The schedule of rates of taxation follows. Section 1390 provides that 'in estimating the gains, profits and income of any person or corporation, there shall be included * * * the amount of sales of all movable property, less the amount expended in the purchase or production of the same * * * and all other gains, profits and income derived from any source whatsoever during said taxation period.' In the face of this language of the statute, the contention that the profits resulting from the sale of stock were not taxable in January, 1931, because they did not wholly accrue during the year 1930, is untenable. The requirement of the statute was that in January, 1931, liability would accrue for taxes on income which was 'received' or 'derived' during the taxation period, which was the year 1930; and this is made even more clear with reference to the sales of movable property when the statute declares that in estimating the profits 'there shall be included * * * the amount of * * * less the amount expended in the purchase.' The legislature did not, in this connection, make any exception of those parts of the gain in value which did not accrue during the taxation year and the court cannot now make the exception." (Record, pages 35 and 36.)

The second contention is purely one of statutory construction.

This Honorable Court, as well as the Supreme Court of the United States, has repeatedly held, in a long line of decisions, that it is desirable that questions involving the construction of territorial statutes be settled by the decision of the Supreme Court of Hawaii. In *Territory of Hawaii v. Gay*, 52 F. (2d) 356, this Honorable Court in affirming a decision of the Supreme Court of Hawaii in respect to a question relating to Hawaiian land tenure, had occasion to enumerate the many decisions enunciating this principle. The court said, at page 359:

“It is desirable that such questions be settled by local legislation and decision. This has been the consistent view of the Supreme Court of the United States (*Kealoha v. Castle*, 210 U.S. 149, 28 S. Ct. 684, 52 L. Ed. 998; *Cotton v. Hawaii*, 211 U.S. 162, 29 S. Ct. 85, 53 L. Ed. 131; *Lewers & Cooke v. Atcherly*, 222 U.S. 285, 32 S. Ct. 94, 56 L. Ed. 202; *Kapiolani Estate, Ltd. v. Atcherley*, 238 U.S. 119, 35 S. Ct. 832, 59 L. Ed. 1229, Ann. Cas. 1916E, 142; *John Ii Estate v. Brown*, 235 U.S. 342, 35 S. Ct. 106, 59 L. Ed. 259; *Cardona v. Quinones*, 240 U.S. 83, 88, 36 S. Ct. 346, 60 L. Ed. 538), and of this court (*Ewa Plantation Co. v. Wilder* (C.C.A.), 289 F. 664, 670; *Territory of Hawaii v. Hutchinson Sugar Plantation* (C.C.A.), 272 F. 856; *Castle v. Castle* (C.C.A.), 281 F. 609; *Halsey v. Ho Ah Keau* (C.C.A.), 295 F. 636; *Notley et al. v. McMillan* (C.C.A.), 16 F. (2d) 273; *Honolulu Rapid Transit Co. v. Wilder* (C. C.A.), 36 F. (2d) 159; *U. S. Fidelity & Guaranty Co. v. Henry Waterhouse Trust Co.* (C.C.A.), 11 F. (2d) 497).”

In *Yoshizawa v. Hewitt*, 52 F. (2d) 411, at page 413, this Honorable Court, in considering a question involving Hawaiian laws respecting members of the board of health, said:

“In view of the fact that the statutory construction here is one of purely local law, and the Supreme Court of the territory has given its interpretation thereof, we see no reason for disturbing the judgment of the latter.

‘Even if the statute is ambiguous, doubt as to its meaning should be resolved in favor of the construction placed upon it by the Supreme Court of the territory. *Clason v. Matko*, 223 U.S. 646, 32 S. Ct. 392, 56 L. Ed. 588; *Ewa Plantation Co. v. Wilder* (C.C.A.) 289 F. 664, 670, and cases there cited.’ U.S. Fidelity & Guaranty Co. v. Henry Waterhouse Trust Co., Ltd. (C.C.A.) 11 F. (2d) 497, 499.

‘* * * The construction placed upon a local law * * * by the highest court of the Territory will not be disturbed by an appellate court. *Kealoha v. Castle*, 210 U.S. 149, 28 S. Ct. 684, 52 L. Ed. 998; *Cotton v. Hawaii*, 211 U.S. 162, 29 S. Ct. 85, 53 L. Ed. 131; *Lewers & Cooke v. Atcherly*, 222 U.S. 285, 32 S. Ct. 94, 56 L. Ed. 202; *John Ii Estate v. Brown*, 235 U.S. 342, 35 S. Ct. 106, 59 L. Ed. 259; *Hawaii County v. Halawa Plantation, Limited* (C.C.A.) 239 F. 836; *Territory of Hawaii v. Hutchinson Sugar Plantation Co.* (C.C.A.) 272 F. 856; *Castle v. Castle* (C.C.A.) 281 F. 609; *Ewa Plantation Co. v. Wilder* (C.C.A.) 289 F. 664; *Halsey v. Ho Ah Keau* (C.C.A.) 295 F. 636.’ *Notley et al. v. McMillan* (C.C.A.) 16 F. (2d) 273.”

In the case of *Ewa Plantation Company v. Wilder*, 289 Fed. 664, in affirming a decision of the Supreme Court of Hawaii involving the construction of the Terri-

torial income tax laws, this Honorable Court said at page 670:

“Another consideration which we consider a conclusive reason for affirming the judgment is that in all cases involving the construction of local territorial statutes, an appellate court must lean toward the interpretation adopted by the Supreme Court of the territory, and will not disturb its decision unless there is clear error. *Cardona v. Quinones*, 240 U.S. 83, 36 Sup. Ct. 346, 60 L. Ed. 538; *Lewers & Cooke v. Atcherly*, 222 U.S. 285, 34 Sup. Ct. 94, 56 L. Ed. 202; *Kealoha v. Castle*, 210 U.S. 149, 28 Sup. Ct. 684, 52 L. Ed. 998. The rule so established has been followed by this court in *Kinney v. Oahu Sugar Co.*, 255 Fed. 732, 167 C. C. A. 78; *Castle v. Castle* (C.C.A.) 281 Fed. 609; *Territory of Hawaii v. Hutchinson Sugar P. Co.* (C.C.A.) 272 Fed. 856; and *In re Bishop's Estate*, 250 Fed. 145, 162 C.C.A. 281.

The judgment is affirmed.”

Likewise, in *Honolulu Rapid Transit Co. v. Wilder*, 36 F. (2d) 159, the construction of an Hawaiian tax law was involved in the decision of the Supreme Court of Hawaii. This court said at page 160:

“The first question thus presented involves the construction of local tax laws, and the rule is well settled that an appellate court will not disturb the construction placed on such laws by the Supreme Court of a territory, except for manifest error. *Fox v. Haarstick*, 156 U.S. 674, 679, 15 S. Ct. 457, 39 L. Ed. 576; *Copper Queen Mining Co. v. Arizona Board*, 206 U.S. 474, 479, 27 S. Ct. 695, 51 L. Ed. 1143; *English v. Arizona*, 214 U.S. 359, 29 S. Ct. 658, 53 L. Ed. 1030; *Notley v. McMillan* (C.A.A.) 16 F. (2d) 273.”

Hill v. Carter, 47 F. (2d) 869, involved the construction of the aforementioned Section 1388, Revised Laws of Hawaii 1925. In affirming the decision of the Supreme Court of Hawaii this Honorable Court said at page 870:

“This case comes within the rule frequently announced by this and other courts, to the effect that ‘an appellate court must lean toward the interpretation adopted by the Supreme Court of the territory, and will not disturb its decision unless there is clear error.’ *Ewa Plantation Co. v. Wilder* (C.C.A.) 289 F. 664, 670. While a dissenting opinion was filed in the court below, we are not impressed that the reasoning of the majority opinion was in error. At least it does not clearly so appear.”

The above mentioned seventeen decisions, all involving appeals from the Supreme Court of Hawaii, are an impressive line of precedents. We respectfully submit that the construction placed upon Sections 1388, 1390 and 1391 Revised Laws of Hawaii 1925, by the highest court of the territory, should not be disturbed by an appellate court. The appellant fails to show any “manifest error” or “clear error” in the construction placed upon the aforementioned territorial income tax statutes by the Supreme Court of Hawaii.

That the appellant realized that his contentions were opposed to the long line of precedents above mentioned, is disclosed by pages 10 and 11 of his brief. He states: “Nor is any question of local statutory construction at issue in this case. In its decision the Supreme Court tacitly conceded that the statute in question could cover

the type of transaction in question * * *." The appellant's last statement has no bearing on the matter,—the statute covers the entire transaction. The Supreme Court of Hawaii decided that the amount of \$408,219.98, paid to the appellant, was not "dividends" within the meaning of that term as it is used in said Section 1391, but was taxable income within the meaning of other sections of the statute. It decided that the said amount was "received" or "derived" by the appellant during the "taxation period," within the meaning of those terms as they are used in said sections 1388 and 1390.

The appellant then proceeds: "On the Supreme Court's own analysis of the problem the question presented is purely and simply: What was the essential character of the transaction in question?—and that is the question which this brief will consider." In determining whether the amounts paid to Lord were "dividends upon the stock" of the appellant the Supreme Court of Hawaii inquired into the findings made by the Territorial Board of Equalization. This necessitated a review of the evidence. After determining that the findings were supported by abundant evidence, the Supreme Court then construed the statutes. Hence, "the question presented" was not "purely and simply" the one mentioned.

After making the foregoing assertions the appellant contradicts the same when he states, on page 38 of his brief, that: "Unquestionably we are here in the realm of 'local statutory instruction' of tax laws." Apparently, "construction" is meant for "instruction."

It is clear from the quotation from *Castle v. Castle*, 267 F. 521, cited on page 11 of appellant's brief, that appellant realized that his contentions were in the realm of local statutory construction. The quotation shows that the Castle case has no application to the case at bar.

2.

THAT THE DECISION OF THE SUPREME COURT OF HAWAII INVOLVES ISSUES AND FINDINGS OF FACT, WHICH FINDINGS ARE SUPPORTED BY SUBSTANTIAL EVIDENCE, AND THAT THE HONORABLE, THE UNITED STATES CIRCUIT COURT OF APPEALS, SHOULD NOT, UNDER SUCH CIRCUMSTANCES, DISTURB THE SAME.

The only law involved in the instant case is the territorial income tax statute. The appellant, as pointed out, maintains that the statute is not involved. Hence, assuming *arguendo* that the appellant's assertion is correct, then the facts must be involved. However, although the appellant argues in his brief to great length about the facts and the findings made thereon, he states on page 10 that: "We should like to make it clear that no question of reviewing conflicting evidence or disturbing any finding of fact is here involved. The facts are undisputed. The question is simply one of determining the intention of the parties from all of those facts, rather than confining our inquiry to the form of the transaction and to some of the

facts." The appellant's dilemma is apparent. If the law is not involved, the findings of fact must be involved.

Moreover, although appellant states in one sentence "that no question" of "disturbing any findings of fact" is involved, he next states that the "question is simply one of determining the intention of the parties." Apparently, he does not realize that "the intention of the parties" is a question of fact. The Territorial Board of Equalization, which had the witnesses before it and observed their demeanor on the witness stand and examined the documentary evidence, found E. J. Lord, Limited, "intended the transaction to be wholly a sale" (Record, page 15). The board based this finding upon both written and oral evidence (Record, pages 15 to 17). The board further found "The records do show that a sale was intended and was consummated." (Record, page 18.)

The Supreme Court in reviewing these findings said: "The main question is, what was the nature of the transaction between the corporation and Lord? As to \$60,000 there is no dispute. It was a restoration to Lord of the capital. As to the remainder, was it received by Lord as a dividend?" (Record, page 27.) The court then proceeded to review the abundant evidence supporting the board's findings (Record, pages 27 to 32) and concluded that the findings were supported by the weight of the evidence. It stated, "The essence of the transaction, as disclosed by the minutes of the corporation, by the formal memorandum of contract, by the formal receipt and by the testimony, is that Lord sold to the corporation and that the

corporation bought back (that is what the word 'redeem' means) from him six hundred shares of stock" (Record, page 32). Thus, whether considered as a review of the board's said findings or as an independent finding, the Supreme Court decided what the parties' intentions were.

That the Supreme Court reviewed and sustained the board's findings as to the "intention of the parties" is clearly shown by its statement "It is not for us to consider now what the parties might have done. What is before us for consideration is, what did they actually do? This is necessarily, in large measure, *a question of the intention of the parties*. The instruments and records above cited are susceptible of only one interpretation in that respect and that is that the parties *understood and intended* that Lord was selling and that the corporation was buying the six hundred shares. Not only was there no reference to a dividend in the records evidencing the transaction, but the statements made tend to exclude and to render impossible the thought of a dividend." (Record, page 33.)

Considered either as a sustaining of the board's findings or as its findings, it is difficult to perceive how the Supreme Court could have been any more definite upon the question of "the intention of the parties." These findings were based upon abundant evidence. The record is replete with evidence supporting the same (Record, pages 41 to 45, 48, 49, 55, 56, 61, 65 to 73, 90 to 93, 100, 104, 108 to 111, 127, 132, 133, 135, 137, 149 to 151, 197, 198, 201, 205, 230 and 268).

This Honorable Court recently decided that intention

is a question of fact. The court also defined the weight to be accorded findings of fact upon appeals from the Supreme Court of Hawaii. It is stated in *Kapiolani Maternity and Gynecological Hospital v. Wodehouse*, 70 F. (2d) 793, at page 801 :

“In a legal action involving issues of fact we have no power to review the finding of a jury or of a judge acting as a jury if there is sufficient substantial evidence to sustain the verdict or decision upon an issue of fact, notwithstanding the fact that there might be an overwhelming weight of evidence on behalf of the appellant and notwithstanding the fact that upon the record we might be disposed to take the opposite view as to the fact in issue to that taken by the trial judge or the jury. This is the general rule applicable to appeals in federal practice, and is applicable to appeals from the Supreme Court of Hawaii. See 28 USCA Sec. 225, and also a recent decision interpreting the statute which allows appeals from decisions of the Supreme Court of Hawaii and of Puerto Rico. *Porto Rico Ry. Light & Power Co. v. Miranda* (C.C.A.) 62 F. (2d) 479. In a case in equity we have power to consider the weight and effect of the evidence, but even in such cases we are largely influenced by the decision of the trial judge, particularly where the witnesses appear in court. We would be very reluctant to overturn a decision of the Supreme Court of Hawaii upon a question of fact where we have the power to do so, and it is because of this reluctance that we have called attention to the fact *that what we are asked to do in this instance is to determine a fact, namely, the intent with which a woman now deceased made a payment of money or caused a payment of money to be made to persons in Hawaii.* We would not hesitate to pass upon this question of fact if it were our duty so to do, but as we understand

our duty it is to decline to pass upon a question of fact in an agreed case and to call to the attention of the Supreme Court of Hawaii that the issue involved is one of fact."

The following authorities show that intent is a question of fact:

"Intent is a question of fact, provable like any other fact in issue.

Intent need not be proven by direct testimony, but may be inferred from the act itself and from the surrounding circumstances."

Vol. 3, *Nichols Applied Evidence*, 2614.

"A man's intention is a matter of fact, and may be proved as such."

Fisk v. Inhabitants of Chester, 74 Mass. (8 Gray) 506;

Kelly v. Cunningham, 83 Mass. (1 Allen) 473;
Commonwealth v. Walker, 108 Mass. 309, 312.

"The state of a man's mind at a given time is as much a fact as is the state of his digestion. Intention is a fact."

Swift v. Rounds, 19 R. I. 527; 35 Atl. 45, 46;
33 L. R. A. 561; 61 Am. St. Rep. 791.

The Supreme Court of Hawaii after carefully considering the record before it in the case made this statement (Record, page 35):

"The conclusion is irresistible that irrespective of what the parties might have accomplished if they had pursued a different course, the transaction as it actually occurred was a sale and purchase and resulted in a profit to Lord in the sale of his stock."

We submit that the questions of fact as to the intention of the parties and as to what was actually accomplished are supported by the great weight of the evidence and should be affirmed.

3.

THAT THE AMOUNTS RECEIVED BY THE APPELLANT FROM THE CORPORATION, E. J. LORD, LIMITED, IN CONSIDERATION OF HIS SELLING TO THE CORPORATION 600 SHARES OF STOCK, WAS NOT A "DIVIDEND" WITHIN THE MEANING OF THAT TERM AS IT IS USED IN SECTION 1391 OF THE REVISED LAWS OF HAWAII 1925.

(a) *The Appellant's Argument.*

The appellant argues, from pages 11 to 37 of his brief, that the consideration received by the appellant was paid by the corporation and received by him as his distributive share of the profits and surplus of the corporation, and, was, therefore, received "as dividends", within the meaning of Section 1391, Revised Laws of Hawaii 1925. This same argument was made to the Territorial Board of Equalization (Record, page 17). The board found that the parties intended, and that the transaction, in fact, was a sale of the stock to the corporation (Record, page 18). It also found that no dividend was received by the appellant.

The same argument was made to the Supreme Court

(Record, pages 26, 32 and 34). The Supreme Court sustained the assessment and the board's findings and reached the same conclusion as the board. Every argument used by the appellant in its brief is disposed of in so careful and in so clear a manner by the Supreme Court that we do not feel that we can improve on its reasoning or language.

The appellant by taking only parts of the evidence away from the greater portion thereof, and by considering it by itself, argues that the board or Supreme Court *might* have found that the amount received by the appellant was intended as a "dividend" within the meaning of the statute. He does not consider all of the evidence. The minutes of the board of directors of E. J. Lord, Limited (Record, pages 134, 136, 138, 199), the carefully drawn agreement of December 13, 1929 (Record, page 65), the agreement of December 26, 1930 (Record, page 90), and the receipts signed by Lord (Record, page 83) are only lightly touched upon. Assuming, but not admitting, that there was evidence upon which to base a finding and that the board *might* have found that the amounts received by the appellant were intended as dividends, the fact remains that there was ample and abundant evidence upon which to base the finding actually made by the board that the amounts received were intended as a consideration for the sale of stock. As heretofore pointed out, such a finding should not be disturbed.

The argument, repeatedly made throughout the appellant's brief, that Lord's share of the net profits of the cor-

poration was 60%, that he agreed to sell his stock for a consideration consisting in part of 60% of the said net profits together with his 60% interest in the corporation's plant and 60% of the profits on uncompleted contracts, is contrary to the evidence. The resolution adopted at the meeting of the corporation's board of directors (Record, page 135), and the formal agreement of December 13, 1929 (Record, page 65) clearly show, as pointed out by the Supreme Court, that a part of the consideration for the sale should be a sum of money *equal* to sixty per cent of the net worth of the corporation, "which net worth must have necessarily included capital as well as the undistributed profits", and "a sum of money *equal* to sixty per cent of the net profits to accrue in the future from contracts then uncompleted. They did not say that it should be sixty per cent of the net profits, but did say that it should be a sum of money equal to sixty per cent of the net profits" (Record, page 33). Why should this careful differentiation be drawn in the resolutions and agreement, if the transaction was intended as a dividend? Assuming that a dividend could have been declared and paid in this manner, the parties would have merely had to state that it was to be sixty per cent of the profits. The language used clearly shows that a sale, not a dividend, was intended. When this foundation is removed from the appellant's argument the entire argument falls.

Moreover, why should any agreement be entered into for the declaration and payment of a dividend? The corporation had paid dividends almost from its inception.

The dividends were declared and paid as dividends are ordinarily declared and paid, namely, by resolutions adopted at its directors' meetings (Record, pages 196 and 198). Such dividends were declared and paid during the years 1929 and 1930 (Record, pages 197 and 198). We submit, that this totally different practice shows that the amounts paid were not a dividend.

Furthermore, as pointed out by the Supreme Court, (Record, page 32) nowhere throughout the corporation's minutes, its books of account, the formal agreement, the receipts, or other evidence was there the slightest reference to a dividend declared or paid. The essence of the transaction, as disclosed by the evidence was that the appellant sold to the corporation his 600 shares of stock.

The Supreme Court also points out that although said Section 1391 provides an exemption in favor of amounts received from a corporation "as dividends upon the stock" of a corporation, the appellant relinquished his stock (Record, page 34).

As stated by the Supreme Court while it may be legally possible for only one shareholder to receive a dividend, that arrangement, when claimed to exist should at least be shown by clear evidence. Black, the other stockholder, received no dividend equivalent to that received by Lord. A dividend could as well have been paid to Black and the money by him later reinvested in his corporation but that was not the course that was followed (Record, page 34).

The reasons for the transaction appear to have been

that, on the one hand, Lord was in poor health and was having domestic difficulties which caused him to wish to retire from business (Record, page 56), while, on the other hand, Black had an ambition to form and control a corporation of his own (Record, page 201). These do not appear to be reasons for declaring and paying a dividend to Lord, but rather reasons for Lord selling his stock so he could retire and so Black could control his own corporation. The testimony of Black quoted and commented upon on pages 13 and 14 of appellant's brief consists of the loose language of a man who stated that he was not an accountant or an attorney (Record, page 201). He made statements, other than that quoted, to the effect that the transaction was a sale of stock by Lord to the corporation. (Record, page 205). Buchholtz's testimony is the same (Record, page 100).

The appellant argues on pages 18 to 21 of his brief, that if the parties had desired simply a purchase and sale of stock they would have taken into consideration all of the elements that determine the value of stock and on that basis would have reached an agreement to pay a fixed sum. It is further stated that "the significant thing about the entire transaction is that there never was any attempt by the parties to reach and agree upon that value." The parties did take into consideration all of the elements that determine value. This all appears from the testimony of appellant's own witnesses—Mr. Peters (Record, pages 57, 58, 60, 76, 78 to 80, 88, 89, 93 and 94). The appellant's brief contains similar statements (Brief, page 20).

The argument contained on pages 21 to 24 of appellant's brief is founded on the premise that there was an agreement to pay and that payment was made to the appellant of "60% of the net profits." As heretofore stated, that was not the case. Moreover, the appellant disregards, in making such an argument, such important evidence as the resolutions adopted by the corporation's directors, the formal agreement of December 13, 1929, and his own receipts.

It is stated on pages 22 and 23 that the parties could have followed one of two courses in determining the amount to be paid to him, namely, estimate the amount of profits on uncompleted contracts, or wait until the profits were determined. We agree with that. However, it does not follow that because the parties agreed that payment should be made when the contracts were completed and the profits were determined that the transaction did not constitute a sale of stock. Such a method is often used in making a sale.

Assuming that the case of *F. G. Lamb*, 14 B. T. A. 814, cited on page 25 of appellant's brief, was correct in respect to the facts there involved, it has no application to the evidence or findings in this case.

On the question of whether or not the payment of money to Lord was a "dividend" or was the consideration for the purchase of stock, the court said: "They did not say that it should be sixty per cent of the net profits but did say that it should be a *sum of money equal to sixty per cent of the net profits.*" (Record, page 33). Section

3361, Revised Laws of Hawaii 1925 (Section 6747, Revised Laws of Hawaii 1935) provides that the directors of a corporation "shall not make dividends except from the profits arising from the business of the corporation". We submit that under territorial law a corporation may not declare a dividend out of the profits not yet earned. Although the Court conceded that it "may be legally possible for one only of two shareholders to receive a dividend, the other consenting to defer his dividend to a later time", still "that arrangement, when claimed to exist, should at least be shown by clear and convincing evidence; and in the case at bar there is no evidence whatever of any such arrangement."

(b) *Appellant's Authorities Discussed.*

There is no merit to appellant's contention that the amount received by him from E. J. Lord, Limited, was a dividend within the meaning of Section 1391, Revised Laws of Hawaii 1925. Most of the cases cited in his brief in support of this contention involve situations wherein dividends were paid to stockholders as a recurrent return on their investment, or wherein payments were made to stockholders upon liquidation or dissolution of the corporation. The appellant has failed to bear in mind the fact that he *ceased* to be a stockholder when the transactions with the corporation were consummated, *and that there was no dissolution* of E. J. Lord, Limited, or of E. E. Black, Limited.

Thayer v. Burr, 119 N. Y. S. 755, at 757, held that

extraordinary dividends declared by a corporation came within the meaning of "dividends" as used in a will directing that the dividends be paid to a certain beneficiary, as distinguished from distributions of "capital."

We have no quarrel with the statement taken from *Trefry v. Putman*, 222 Mass. 522, 116 N. E. 904 at 912, as given in Appellant's Brief (pages 26 and 27), but we do feel that the statement would be clarified by calling the court's attention to the language immediately following the statement:

"Moreover, it is expressly provided in the income tax law (section 2) that:

'No distribution of capital, whether in liquidation or otherwise, shall be taxable as income under this section: *but accumulated profits shall not be regarded as capital under this provision*.'

It is submitted that the term "dividends" as used in *University v. N. C. R. R. Co.*, 76 N. C. 103, 22 Am. Rep. 671 at 672, can have no application or bearing upon the definition of dividend as that term is used in our income tax laws.

The case of *Eyster v. Centennial Board*, 94 U. S. 500, 24 L. Ed 188 at 189, has no application as shown by the sentences following the quotation used by appellant.

The *Spencer, Smith, Hartley, Norton, Travis, Thompson* and *Barnes* cases (brief, pp. 27-28) contain various rules and definitions concerning dividends issued in fact or by operation of law, but they have no application to the facts of this case.

The factual situation in *Hadley v. Commissioner*, 36 F. (2d) 543, prompts us to make but one comment. The Court decided that under the circumstances presented a tax assessment against a stockholder was proper because money credited to his account was a dividend received as the term "dividend" is defined in section 201 (a) of the Revenue Act of 1918. To the same effect are *Chattanooga Sav. Bank v. Brewer*, 17 F. (2d) 79, and *Christopher v. Burnet*, 55 F. (2d) 527.

There is nothing in *Commissioner v. Ward*, 65 F. (2d) 758, to sustain the appellant's contention that the money received by the appellant was a dividend. The case involves the federal income tax law. (Revenue Act of 1924). The term "dividend" as defined in Section 201 (a) and Section 234 (a) thereof provides a deduction of amounts received as dividends in computing net income. The Treasury Department ruled that profits of a building and loan association, periodically credited to its members, and payable to the member upon his retirement from the association, are to be treated as "dividends" within the meaning of Section 201 (a). This is merely authority for the rule that accumulated profits credited periodically until building and loan shares mature constitute dividends under the federal law.

The case of *Phelps v. Commissioner*, 54 F. (2d) 289, is hereinafter discussed.

That the appellant's authorities have but little bearing upon the instant case is disclosed by the statement contained on page 30 of his brief, that

“We know of no state cases dealing specifically with the problem here involved. Most of the federal cases are inapplicable for the reason that almost every Revenue Act has made specific provision for the treatment of cases of retirement of stock or corporate dissolution. Obviously the fact that Congress chooses to treat gains derived from these transactions in a certain way either as dividends or as capital gains—sheds no light on the question now at issue.”

Assuming for the purpose of argument that a corporation may legally pay a dividend to one of its stockholders and not to the others, we submit that the Supreme Court of Hawaii correctly decided that if such an arrangement is claimed it should be shown by clear and convincing evidence. It said: (Record, page 34) “in the case at bar there is no evidence whatever of any such arrangement”.

*c—The Amounts Paid to the Appellant
were not a “Dividend”.*

1. *Basis of assessment.*

The tax assessment against the appellant was predicated upon the following grounds:

(1) That the business of appellant in the year 1926 constituted a capital asset to him;

(2) That when he sold his business to E. J. Lord, Limited, a corporation, and a separate entity, he received in exchange therefor an equivalent capital asset, to-wit, 600 shares of the capital stock of E. J. Lord, Limited;

(3) That, as defined in Section 6729 of the Revised Laws of Hawaii 1935 (Revised Laws of Hawaii 1925, Section 3350), such shares of stock are deemed in law to

be personal property, and as personal property the same were held by appellant until he sold the same to the corporation, E. J. Lord, Limited;

(4) That under the provisions of the territorial income tax law and particularly that part of Section 1390, providing as follows: "the amount of sales of all movable property, less the amount expended in the purchase of or production of the same", the difference between what the taxpayer paid for these shares and what he sold them for, to-wit, \$398,224.40, constitutes a taxable gain. It was conceded by the witness Camp, tax expert for the appellant, that the territorial income tax law imposes a tax on capital gains (Record, page 152). In fact all past administration of the income tax law has recognized the propriety of a tax on capital gains and deductions in case of capital losses. This view of the law was upheld in the case of *Ewa v. Wilder*, 26 Haw. 299, affirmed in 289 Fed. 664. If, therefore, this stock was a capital asset to appellant and the transaction by which he disposed of that capital asset constituted a sale of his capital asset, it must follow that the gain resulting from such sale can be properly taxed.

The appellant, in his contention that a sale did not take place, has confused his status as a stockholder with that of the corporation. It is universally recognized that stock in a corporation constitutes personal property to the stockholder. Declaratory of the common law in this respect is Section 3350, Revised Laws of Hawaii 1925 (Section 6729 of the Revised Laws of Hawaii 1935). The

interest thus accruing to a stockholder by virtue of ownership of shares is separate and distinct from any interest in property owned by the corporation and vice versa. In the case of *Klein v. Board of Tax Supervisors of Jefferson County, Kentucky*, 282 U. S. 19, 51 S. Ct. 15, 75 L. Ed. 140, it is held that "stockholders are not the owners of the property of the corporation, the corporation itself being a person, whose ownership is a nonconductor, that makes it impossible to attribute an interest in its property to its members." Likewise in the same case, it is held that a state may tax both a corporation and the holders of the stock, and that the same will not constitute double taxation. In other words, there is no relationship between taxation of the stock of a corporation and taxation of the corporation property.

The general definition of "sale", contained in the Uniform Sales Act, Section 7360, Revised Laws of Hawaii 1935, is apropos as indicating what is generally understood by a sale. That definition is as follows:

"A sale of goods is an agreement whereby the seller transfers the property in goods to the buyer for a consideration called the price."

In the case at bar, we have E. J. Lord, one entity, as the "seller", and E. J. Lord, Limited, a corporation, another entity, as the "buyer", engaging in a transaction whereby Lord as the "seller" transfers the property in stock owned by him to the corporation as the "buyer" for a consideration of \$468,219.98. The record is replete with evidence, clearly showing that a sale took place. The

Board of Equalization came to this conclusion after hearing all the witnesses and reviewing all the evidence. (Record, pages 15-17). The Supreme Court made similar findings.

In further support of this conclusion the record shows that no dividend was declared by the company representing the payment made to the appellant (appellant's witness Buchholtz, Record, pages 275-277).

In harmony with this reasoning, we desire to call the attention of the Court to the case of *Langstaff v. Lucas*, 9 F. (2d) 691, affirmed by the Circuit Court of Appeals for the Sixth Circuit, 13 F. (2d) 1022, and certiorari denied by the Supreme Court of the United States November 1, 1926, 71 L. Ed. 858, 273 U. S. 722. This case will be hereinafter discussed. The reasoning used by the court in that case is strikingly applicable to the issues at bar.

(d) *No "liquidating dividend" was paid.*

Throughout the hearing of this case before the Territorial Board of Equalization and later before the Supreme Court, the appellant contended that the payment made by the corporation to the appellant was in the nature of a liquidating dividend, and, as such came within the class of dividends specifically exempted from taxation under the provisions of said Section 1391 of the Revised Laws of Hawaii 1925, reading as follows:

"Provided, further, that in assessing income of any person or corporation there shall not be included the amount received from any corporation as divi-

dends upon the stock of such corporation if the tax of two per centum has been assessed upon the net profits of such corporation as required by this Chapter, nor any bequest or inheritance otherwise taxed as such."

Judging from the cases cited on pages 26 to 37 of appellant's brief the same contention is now being made to this Honorable Court.

Before proceeding to analyze the appellant's contention, the court's attention is particularly called to that part of the above proviso reading as follows: " * * * as dividends *upon* the stock of such corporation * * * ". We particularly emphasize the word "upon", because as this word is used, it does not allow for the substitution of any words such as "in exchange for", or their equivalent, as would be required if we are to accept the contention of the appellant.

In an effort to bring appellant's income within the four corners of the exemption, he pierces the corporate veil, and quotes voluminously from the cases construing the federal law. We feel, as did the Supreme Court, that appellant is attempting to create a dividend where none in fact existed. His task is troublesome because in no part of the transaction between appellant and the corporation was the term "dividend" ever mentioned. On the contrary when appellant filed his federal income tax return, the transaction was classified as one involving the sale of capital assets (Record, pages 164-165) and a tax was paid by the appellant on the basis of a gain realized from such sale, computed in the same manner as the tax assessor in the instant case has computed the territorial tax.

It is stated by witnesses for the appellant that the reason why the transaction was not described as a distribution of liquidating dividends was because the appellant would have had to pay a higher tax because the gain resulting from the sale of capital assets carries but the normal tax, whereas a liquidating dividend is subject to not only the normal tax, but to a surtax in addition (Record, page 165). We submit that the appellant could only classify the transaction as a sale of capital assets.

Under the federal law a condition precedent to a liquidating dividend was dissolution. In the case at bar there was no dissolution of E. J. Lord, Limited, and accordingly no liquidating dividend can be claimed.

Great stress is asked by the appellant to be placed upon *Phelps v. Commissioner*, 54 F. (2d) 289. However, we believe and submit that this case supports the position of the Territory rather than the contention of the appellant. First, there was involved a question of fact which was determined by the Board of Tax Appeals. Second, the federal income tax law was being construed, the provisions and theory of which are not at all parallel to the territorial statute.

The decision of the Court says in part at page 292:

"It is quite probable, as petitioners suggest, that the sale of stock to a corporation by one shareholder would be considered as a sale rather than as a liquidating dividend, for the act of one of several stockholders could not well be considered as evidence of an intention of all the stockholders; but in the instant case the Board evidently considered the concerted

action of all the directors and stockholders in the disposition of practically all the stock as *probative of intention of the company to liquidate*, and we think the Board was right in so considering it.

The intention of the parties weighs heavily in determining the nature of such transaction, and this intention may be fairly arrived at in the instant case by the acts of the parties. On December 27, 1922, the determination to act was first expressed, and it was made of record by resolution. It authorized the president to purchase for the company such amounts of the company's capital stock and at such prices—not to exceed \$130 a share—as he might deem fit. Within four days from that date he bought and paid for all the stock, except 300 shares of his own, and at the highest price authorized. Within less than two weeks from the date of the resolution the board of directors had authorized a reduction of the capital stock to 300 shares, all of which were owned by Mr. Phelps. *The entire transaction was remarkable for its celerity and lack of discord, and impels the conclusion that it was a voluntary distribution by the stockholders of all the assets of the company.* The fact that Mr. Phelps received money for part of his stock and retained the remaining outstanding stock cannot militate against such conclusion. He was thereby, in effect, the owner of the undisposed of assets of the corporation, which consisted only of the Jefferson street property. Technically, as between the stockholders and the corporation, it was not a complete liquidation in the sense that all the assets had been converted into cash and distributed; but as between the stockholders themselves, for all practical purposes, there was in effect a complete distribution, which was evidently made by agreement of the parties and one which they were fully authorized to make. *Breslin v. Fries-Breslin Co.*, 70 N. J. Law, 274, 58 A. 313; *Joseph Goodnow & Co. v. Commissioner*, 5 B. T. A. 1154; *F. G. Lamb v. Commissioner*, 14 B. T. A. 814.”

We respectfully submit that appellant's statement on pages 31 and 32 of his brief is erroneous. It is said :

"The Circuit Court of Appeals held, looking through the form of the transaction to its substance, that the essence of the transaction was not a sale of stock but was, to the extent surplus was distributed, a distribution of profits in the nature of a dividend."

The Circuit Court of Appeals did not in effect so hold. It did hold that the Board of Tax Appeals rightly classified the transaction according to the facts presented.

"In each of the above cases the Board and the court, respectively, classified the transaction before it according to the facts presented, and we think rightly so. *Of course the facts in each case are different, and each case must be governed by its own facts.* It may be said, however, that the cases cited by petitioners herein support the rule that it is the duty of both the Board and the court to classify such transactions consistently with the facts presented. It will be observed that in the cases just discussed there was no effort on the part of any petitioner to give any particular name to the transaction until the hearing was had before the commissioner. In the instant case the order of procedure is somewhat changed, in that petitioner had given a name to the transaction before the issue was formed. But names mean nothing unless they are supported by the facts."

And this language is particularly applicable in the present case. We have the decision of the Board of Equalization which found as a fact that the transaction between Lord and the Company was a sale and not a distribution to him as a dividend. If Lord had, for the purpose of

escaping taxation, chosen to call the transaction a dividend and not a sale, and the board had so found, the question being one of fact would be closed, unless, of course, its decision was obviously incorrect. As the court said: "names mean nothing unless they are supported by the facts." The finding must stand.

In *Hellmich v. Hellman*, 276 U. S. 233, 72 L. Ed. 544, 56 A. L. R. 379, the Supreme Court of the United States in construing the Revenue Act of 1918, and Treasury Regulations 45 promulgated under the Act, held that distribution to stockholders of a corporation during its liquidation, out of gains and profits accumulated since February 28, 1913, are regarded as payments for stock and should be taxed to the stockholders as profits and not as "dividends" exempt from the normal tax. The Court said that the Treasury Regulations correctly interpreted the act as making section 201 (a) applicable to a distribution made by a going corporation to its stockholders in the ordinary course of business, and section 201 (c) applicable to a distribution made to stockholders in liquidation of the corporation, and that such interpretation was in accord with the rulings of the Board of Tax Appeals. A portion of the Treasury Regulation under discussion reads as follows:

"A distribution in liquidation of the assets and business of a corporation, which is a return to the stockholder of the value of his stock upon a surrender of his interest in the corporation, is distinguishable from a dividend paid by a going corporation out of current earnings or accumulated surplus when de-

clared by the directors in their discretion, which is in the nature of a recurrent return upon the stock.”

Although there is no question of liquidation in the case at bar, still the analogy is of importance in determining the present issue. The court’s statement regarding the definition of “dividend” as that term is used in the income tax law, is clear. It said:

“It is true that if sec. 201 (a) stood alone its broad definition of the term ‘dividend’ would apparently include distributions made to stockholders in the liquidation of a corporation—although this term, as generally understood and used, refers to the recurrent return upon stock paid to stockholders by a going corporation in the ordinary course of business, which does not reduce their stock holdings and leaves them in a position to enjoy future returns upon the same stock. See *Lynch v. Hornby*, 247 U. S. 339, 344-346, 62 L. Ed. 1149, 1151, 38 Sup. Ct. Rep. 543; and *Langstaff v. Lucas* (D. C.) 9 F. (2d) 691, 694.”

No valid reason has been given by the appellant to show why the term “dividend”, as used in the case at bar, should have any other meaning than its general and ordinary signification. The Supreme Court comments upon this. (Record, page 34.) Annual dividends were declared by E. J. Lord, Limited, from the time of its incorporation. (Record, pages 196-198.) In 1929 the company paid dividends totalling \$150,000 to its stockholders, and in 1930 it paid a \$25,000 dividend to E. E. Black. The appellant’s witness, George Buchholtz, answered in the affirmative a question asked, referring to the \$25,000 dividend,

“That was the only dividend of any character whatsoever declared in the year 1930?” (Record, page 198.)

We have no quarrel with the federal statutes or federal authorities cited by counsel interpreting the federal statute. To the extent the federal statute is comparable to our own statute, then and there only, are we ready to concede that it is of value in this controversy.

The term “liquidating dividends” first made its appearance in federal legislation subsequent to the year 1918. The necessity therefor arose because property belonging to taxpayers was being transferred to corporations of which the taxpayers were stockholders, they receiving stock in exchange for property transferred. Under the principle then accepted by the federal government, that no gain or loss arose from such an exchange, the result was that fictitious values of the property, so exchanged, were put on the books of the corporation and subsequent sales of the property so transferred to the corporation reflected gains or losses only in relation to these fictitious values. In order to correct this abuse, the Congress of 1921 passed an act closing the gap, and thereunder, regardless of what terminology may be used, the federal government taxes a normal tax and surtax against any distribution made by a corporation in liquidation. The great majority of the cases cited by the appellant deal with the efforts of the courts to uphold the congressional enactment and the books are full of decisions holding that distributions made in liquidation are really liquidating dividends, subject to the normal and surtax as that term is used and

defined in the federal statutes, and, in sustaining the tax, the courts have had occasion to brush aside subterfuges and all manner and means of circumventing devices. Consequently, when the federal government, as appears from the record (Record, page 165), accepted the return of the taxpayer as reflecting a sale of capital assets, it may be conclusively assumed that the transaction in question did not reflect a "liquidating dividend", as that term is known and used in the federal law. Otherwise the federal government would have refused to accept the return and would have classified the transaction as one of distribution of liquidating dividends and assessed the greater tax accordingly. But the taxpayer contends the payment was really a liquidating dividend as that term has been used in federal legislation. Assuming this premise, what value has it in the present controversy? We will later show that the term had no relation to the term "dividend" as that term was used in earlier federal statutes, particularly in the 1913 and preceding statutes (See *Langstaff v. Lucas*, 9 F. (2d) 691, *post*).

Turning to the territorial income tax law we desire to call the attention of the Court to the date of the enactment of the exemption proviso in question, to-wit, Section 1391 of the Revised Laws of Hawaii 1925. This date is 1901—many years before the term "liquidation dividend" was known to the federal law. There is no language in the territorial act justifying the contention that liquidating dividends is synonymous with the term "dividend" as used in Section 1391. It cannot be found because the term

“liquidating dividend” was unknown in taxation councils at the time the local statute was enacted. And, see Section 3361, Revised Laws of Hawaii 1925 (Section 6747 of the Revised Laws of Hawaii 1935), a statute in *pari materia* relating to dividends as that term was understood at the time the income tax statute became law; and see testimony of Harold C. Hill (Record, pages 257-261), and of Henry Glass (Record, page 234). We will not prolong this line of argument in view of the fact that the reasoning in the case of *Langstaff v. Lucas*, 9 F. (2d) 691, conclusively disposes of the contentions of the taxpayer. There it appeared that the Langstaff-Orm Manufacturing Company, a Kentucky corporation, had a surplus accumulated since the federal income tax law went into effect, and shortly before December 1, 1919, the two stockholders, owners of all the stock, decided to liquidate the corporation and transfer all of its assets to a partnership to be called the Langstaff-Orm Lumber Company, the two owners of the stock to become the owners of the partnership business. It was provided in the agreement that no part of the assets, including the surplus, so distributed should be to the use of the shareholders individually, but only to the use of the partnership. There was assessed against the plaintiff on account of his own half of the surplus received a normal tax and a surtax. The plaintiff paid the taxes under protest and brought an action to recover the amount so paid.

“By an amended petition the plaintiff asserts that, even if the one-half of the surplus assignable to his

stock in the corporation should be treated as taxable income accruing to him in the year 1919, yet it was *income in the nature of a dividend*, and therefore was not subject to the normal tax for that year, which amounted to \$1,711.21 of the total of \$3,886.68 assessed against him, and that therefore in any event he is entitled to recover against the collector the sum of \$1,711.21, with interest from the date of its payment. The case is submitted on demurrer to the petition as amended."

It was held that the transfer of the corporation assets was made to the stockholders individually, and was taxable as income as to the surplus. The Court stated (at page 693) that plaintiff's contention that the transfer to the partnership in accordance with the agreement did not amount to a transfer to the individuals violated the most elementary principles of partnership law. And in disposing of the plaintiff's contention that the surplus received by him should be considered as a dividend, the Court said, commenting on Section 201 of the Revenue Act of 1918:

"This section strips distributions made to stockholders in liquidation of a corporation of all disguises and declares that they shall be considered for what they in effect are—purchases of all their outstanding stock by the liquidating corporations, and not dividends as generally understood, and as defined in section 201, subsection (a), and as used in section 216. So construed, subsection (c) of section 201 puts the stockholder who holds his stock up to the time of liquidation, and then in effect sells it to the corporation, upon exactly the same footing as the stockholder who sells his stock to another during the operating life of the corporation. The latter unquestionably, under the act of 1918, was required to pay both the

normal and surtax upon any profit realized by him in the transaction. That is all the former was required to do under the act as here construed.

For the reasons stated, the court is forced to the conclusion that it was not intended by Congress that so-called liquidating dividends, to the extent of the profit received, should escape the normal tax. It necessarily follows that the court is of the opinion that the plaintiff has stated no cause of action, and the demurrer to the petition will be sustained."

As defined by Mr. Justice Pitney in the case of *Lynch v. Hornby*, 247 U. S. 339, 38 S. Ct. 543, 62 L. Ed. 1149, the word dividend as used in the Act of 1913 means:

"In short, the word 'dividends' was employed in the act as descriptive of one kind of gain to the individual stockholder; dividends being treated as the tangible and recurrent returns upon his stock, analogous to the interest and rent received upon other forms of invested capital."

As the court said, "in other words, it is earnings paid to him by the corporation upon his invested capital therein, without wiping out his capital".

The case of *Zimmers v. City of Milwaukee*, 189 Wis. 269, 206 N. W. 178, is applicable to the case at bar. The plaintiff, Zimmers, and his family owned one-half of the outstanding capital stock of the Kalt-Zimmers Manufacturing Company. The other one-half was owned by members of the Kalt and Casper families. Dissension arose between the plaintiff and his family on the one hand and the Kalts and Caspers on the other hand, and in 1920 the plaintiff elected to sell his stock at a price fixed by the

Kalt-Casper group, which offer to sell was an option to the plaintiff arising out of the written agreement between the parties. The company had been prosperous and had a considerable surplus on hand. The purchase price was agreed upon and was paid from the assets of the company in the form of Liberty Bonds, War Saving Stamps, a note secured by a mortgage on the company's property, certificates of indebtedness belonging to the company and a promissory note of Kalt and Casper. This action was approved by a resolution adopted at a meeting of the board of directors. After the closing of the transaction the plaintiff signed a statement which recited the receipt by him of the Kalt-Casper promissory note "as constituting the balance of the purchase price" of the shares. The plaintiff made no recital of this transaction in his income tax return for 1920, and he was assessed and paid under protest an income tax on a profit of \$60,638.52 which the assessing officers determined he had realized as a result of the sale of his shares. In an action to recover the tax paid the circuit court decided in favor of the defendant, and this decision was upheld by the Supreme Court.

It was contended on behalf of the plaintiff that the proceedings should be considered as a distribution in the nature of a dividend or a distribution of surplus assets among its stockholders and therefore, the company having paid an income tax upon the receipts and revenues making up such surplus, the dividends paid would not be subject to an income tax. It was further urged that the court go behind the mere face of the proceedings and determine

the real substance of the transaction. The court in reply to this contention said :

“The language used in the recitals of the minutes of the proceedings, and of the resolution adopted by the stockholders and by the board of directors, makes no statement to the effect that it was thereby and then intended to distribute, as a dividend, the corporate assets to the respective stockholders as such and in proportion to their holdings. All the writings, including the declaration by plaintiff of October 28th in the adjustment of interest recited above, speak of the transaction as a purchase by the Kalt-Casper party of the shares of stock held by the Zimmers family, and of the entire amount to be paid as the purchase price.

There is no showing made of entries on the books of the corporation, at or after the time of the transaction, tending to indicate that, by appropriate entries, it was treated by the company at that time as a dividend, as distinguished from an advance out of the property of the company for the furtherance of a purchase by one set of stockholders of the stock held by the other set, in order that the internal dissensions that had so long troubled the company might be ended — a consummation which the corporation might well and devoutly wish.

The oral testimony, if such could properly be considered in determining the real effect of the transaction, was on both sides of the question ; the plaintiff testifying that it was the purpose at that time to distribute the surplus of the company as a dividend. Mr. Casper and his counsel, who took part in the transaction, testified to the contrary. On that feature of it, therefore, of course, *it presented a question of fact, and the findings of the taxing officers with reference to such manifestly could not be disturbed.*”

And the following excerpts from the decision are deemed important as bearing on the case at bar :

“Stress is laid by plaintiff upon the recital in the findings by the trial court to the effect that, upon the acceptance of the proposal by the Zimmers party that the Liberty Bonds, stamps, certificates of indebtedness, note, and mortgage were delivered by said corporation pursuant to said resolution, and the title to the same absolutely and irrevocably passed to and vested in the Zimmers faction, together with the promissory note of Kalt and Casper, arguing therefrom that it is in effect such a finding of fact, which must lead to the legal and logical conclusion that the title to this property passed directly to the plaintiff from the corporation, and never reached the person buying the Zimmers stock, and that this effect could only be reached by treating this as a dividend. We cannot, however, so construe this finding, nor could it control, if treated as a conclusion of law, because, if such, it would be, as we have indicated above, incorrect.

We are therefore satisfied that no other reasonable construction can be given to the transaction between the interested parties in October 1920, than that it was a purchase outright at the designated price per share of the entire holdings of the Zimmers family by the Kalt-Casper party, in which transaction the company on its own behalf and for its own interest assisted in advancing to the Casper-Kalt party which happened to be the buyer under the option, thereafter exercised, some of its assets and pledged its credit.”

4.

THAT THE AMOUNT RECEIVED BY THE APPELLANT FROM THE CORPORATION, E. J. LORD, LIMITED, WAS TAXABLE INCOME DERIVED FROM THE SALE OF 600 SHARES OF STOCK.

The arguments and authorities contained on pages 27 to 53 hereof.

5.

THE EXEMPTION CLAIMED BY THE APPELLANT SHOULD NOT BE CONSTRUED IN HIS FAVOR, BUT SHOULD BE STRICTLY CONSTRUED IN FAVOR OF THE GOVERNMENT.

The result of appellant's contention is that the statute in question should be construed favorably to the taxpayer. It is submitted that the construction claimed by the appellant is unsound and unsupported by persuasive authority in so far as it is claimed to be applicable to the issues of this case.

Corliss v. Bower, 281 U. S. 376, 74 L. Ed. 916.

Cooley on Taxation, Vol. 1 (4th Edi.) 1403-1408,

clearly crystallizes the general principle of law applicable as follows:

"Sec. 672. *Strict construction—Rule Stated.* An intention on the part of the legislature to grant an exemption from the taxing power of the state will

never be implied from language which will admit of any other reasonable construction.

* * *

“Exemptions are never presumed, the burden is on a claimant to establish clearly his right to exemption, and an alleged grant of exemption will be strictly construed and cannot be made out by inference or implication but must be beyond reasonable doubt. In other words, since taxation is the rule, and exemption the exception, the intention to make an exemption ought to be expressed in clear and unambiguous terms, it cannot be taken to have been intended when the language of the statute on which it depends is doubtful or uncertain; and the burden of establishing it is upon him who claims it. Moreover, if an exemption is found to exist, it must not be enlarged by construction since the reasonable presumption is that the state has granted in express terms all it intended to grant at all, and that unless the privilege is limited to the very terms of the statute the favor would be extended beyond what was meant.” (Citing many authorities including United States Supreme Court and numerous States.)

And see *Tax Assessor vs. Wood*, 18 Haw. 485:

“The proposition that exemptions from taxation are strictly construed, in other words, that taxation is the rule and exemption the exception is well settled. *Bishop v. Gulick*, 7 Haw. 627, 630; *O. R. & L. Co. v. Shaw*, 12 Haw. 76. As the United States supreme court puts it, ‘a doubt is fatal to the claim’ of exemption.”

See also *O. R. & L. Co. vs. Shaw*, 12 Haw. 76, 77. *Bishop vs. Gulick*, 7 Haw. 627, 630.

Under the rule of strict construction, it is obvious that the exemption claimed must be denied.

6.

THE COURT DID NOT ERR IN HOLDING THAT THE DIFFERENCE BETWEEN THE COST OF APPELLANT'S STOCK AND THE AMOUNT HE RECEIVED THEREFOR WAS TAXABLE.

(a) *The rule of Darlington v. Gray is not applicable to the case at bar.*

As heretofore stated, appellant's argument, contained on pages 37 to 46 of his brief, is founded upon matters having to do with the construction of Hawaiian statutes. The construction placed upon the statutes by the Supreme Court (Record, pages 35 to 37) is sound, and, we submit, should be followed.

As there stated :

“* * * In the face of this language of the statute, the contention that the profits resulting from the sale of stock were not taxable on January 1931, because they did not wholly accrue during the year 1930, is untenable. The requirement of the statute was that in January 1931, liability would accrue for taxes on an income which was ‘received’ or ‘derived’ during the taxation period, which was the year 1930; and this is made even more clear with reference to the sales of movable property when the statute declares that in estimating the profits ‘there shall be included * * * the amount of * * * less the amount expended in the purchase’. The legislature did not, in this connection, make any exception of those parts of the gain in value which did not accrue during the taxation year and the court cannot now make the exception.”

Much that has been said on pages 36 to 39 hereof under the topic "basis of assessment" is applicable to appellant's argument.

The case of *Gray v. Darlington*, 15 Wall. 63, 21 L. Ed. 45, is relied upon by the appellant as decisive of the case at bar on the proposition that the Supreme Court of Hawaii erred in holding that the difference between the cost of his stock in 1926 and the amount he received therefor in 1930 was taxable. The statute in the *Darlington* case taxed "gains, profits and income *for* the year ending the 31st of December next preceding the time for levying, collecting and paying said tax". That this case has not been questioned or modified is correct. *Lynch v. Turrish*, 247 U. S. 219, 62 L. Ed. 1087. For this reason appellant argues that it is binding in the case at bar, and he attempts by placing emphasis on certain phrases appearing in the Act of Congress involved in the *Darlington* case (Act approved March 2, 1867) and by doing the same thing with respect to the territorial statutes here involved (Sections 1388 and 1390, Revised Laws of Hawaii 1925), to place the same construction on both.

It was held in *Hays v. Gauley Mountain Coal Co.*, 247 U. S. 189, 62 L. Ed. 1061, that the *Darlington* case was not controlling because the language of the statute there involved was different in material particulars. In distinguishing the two statutes the court said:

"Gains, profits, and income *for* the year ending the thirty-first day of December next preceding (Act of 1867) conveys a different meaning from the entire net income * * * *received by it* * * * *during* such year

(Act of 1909). The former expression, as this court held (15 Wall. 65, 21 L. Ed. 46), denoted 'such gains or profits as may be realized from a business transaction begun and completed during the preceding year', with the exceptions already mentioned. The expression 'income *received* during said year', employed in the Act of 1909, looks to the time of realization rather than to the period of accrument, except as the taking effect of the act on a specified date (January 1, 1909) excludes income that accrued before that date."†

The Hawaii Supreme Court noted and followed this distinction, citing the *Hays* case (Record, page 36). It was pointed out by the Court that the statute under consideration in the *Hays* case (Act of Congress of 1909) taxing income received by the taxpayer "*during* such year" is the "equivalent of the expressions used in our statute for the admeasurement of taxable income."

In *Ewa Plantation Company v. Wilder*, 26 Haw. 299, the tax assessor relied upon the *Darlington* case to support his contention that where securities had been purchased by the taxpayer during the years 1904-1917 for the par value of \$100 per share, and were sold by the taxpayer at a loss of \$60 per share in 1920, that the losses were *ascertained* in 1920, although not *sustained* in that year. The assessor contended that such losses could not be deducted from the taxpayer's total income received in 1920; that only losses sustained during the taxation period could be deducted. This is the converse of the situation now before this Court. The Supreme Court of Hawaii in the *Ewa Plantation* case held that the losses sustained by the tax-

† Emphasis supplied by the Court.

payer in 1920, through the sale of the securities, were deductible as losses in computing its income taxes for that year. Speaking of the *Darlington* case it said :

“The United States Supreme Court in a recent decision (*Hays, Collector, v. Gauley Mountain Coal Co.*, 247 U. S. 189) distinguished the corporation excise tax of August 5, 1909, from the act of March 2, 1867, under which *Gray v. Darlington* was decided, and held that where property is sold by a corporation at an advance over the original purchase price the amount of the advance must be deemed to be a gain or profit for the purpose of computing income for taxation under the federal statute. See also *Merchants' Loan & Trust Co. v. Smietanka*, decided by the federal Supreme Court March 28, 1921, and Holmes, Fed. Taxes, p. 632.” * * * (26 Haw. at 319).

“There is a dearth of federal judicial authority on the question before us, due no doubt to the fact the federal government has uniformly acquiesced in the position here assumed by the taxpayers and which we deem to be the only fair and practicable method of ascertaining losses of the nature involved. It is a notorious fact that during the last decade all stocks and bonds throughout the world have violently fluctuated with the greatest frequency, often changing in value from time to time with kaleidoscopic rapidity. This fact alone would render it impossible to determine the actual time at which the losses were sustained by the taxpayers, if the method of ascertaining those losses proposed by counsel for the assessor were adopted, and would deprive the taxpayers of the benefit of deductions from gross income caused by losses which it is conceded they actually sustained.” (26 Haw. at 321).

The Supreme Court of Hawaii in the instant case did

not overrule, *sub silentio*, *Castle v. Tax Assessor*,† 18 Haw. 129, as stated by appellant (brief, page 38), but it followed the ruling in *Ewa Plantation Company v. Wilder, supra*, affirmed, 289 Fed. 664. It also appeared in the *Ewa Plantation* case as stated by the court below (Record, page 36), that the plantation received a lump sum settlement in 1920 for damages to crops sustained in that year. A portion of the damaged crops involved were harvested and sold subsequent to 1920. The taxpayer took the position that this payment was attributable to the years in which the damaged crops were sold, and should be taxed as income for such years. Under the authority of the same taxing statute here involved, the court held that the money so received was taxable as income received in 1920. In its decision of that case the Hawaiian Supreme Court said, at page 319:

“The decision of this court *In re Appeal of J. B. Castle, supra*, asserts a mere conclusion, entirely devoid of any reasons therefor except that it is based upon the decision in *Gray v. Darlington, supra*, a case involving the construction of the Revenue Act of 1867 (14 Stat. 477, c. 169).”

This court in upholding the construction placed upon the statute by the Supreme Court of Hawaii in the *Ewa Plantation* case, said:

“The statute plainly provides that the return of the taxpayer shall include all ‘gains, profits and income, derived from any source whatsoever during said taxation period.’ Rev. Laws Hawaii 1915, Sec. 1307. The inference is not deducible from the deci-

† Also referred to as “*In re Appeal of J. B. Castle*.”

sions of the Supreme Court of Hawaii that income actually received in one year is not taxable as income of that year but is to be carried into the income of another year." (289 Fed. at 667.)

See, also, 61 C. J., p. 1580, Sec. 2331.

The time when gains are deemed to have been realized under the taxing laws is, we submit, correctly stated in *McLaughlin v. Alliance Ins. Co.*, 286 U. S. 244, 76 L. Ed. 1083, wherein it appears that:

"* * * Realization of the gain is the event which calls into operation the taxing act, although part of the profit realized in one accounting period may have been due to increase of value in an earlier one. While increase in value of property, not realized as gain by its sale or other disposition, may, in an economic or bookkeeping sense, be deemed an addition to capital in a later period, see *Merchants' Loan & T. Co. v. Smietanka*, 255 U. S. 509, 65 L. Ed. 751, 15 A. L. R. 1305, 41 S. Ct. 386, it is nevertheless a gain from capital investment which, when realized, by conversion into money or other property, constitutes profit which has consistently been regarded as income within the meaning of the Sixteenth Amendment and taxable as such in the period when realized." (76 L. Ed. at 1086.)

In *Merchants' Loan & T. Co. v. Smietanka*, 255 U. S. 509, 65 L. Ed. 751, 15 A. L. R. 1305, 41 S. Ct. 386, the *Darlington* case and *Lynch v. Turrish*, *supra*, were relied upon to support a recovery of taxes paid under the Act of Congress, approved September 8, 1916, as amended by the act approved October 3, 1917, and the Supreme Court of the United States in refusing to follow those cases said:

"Gray v. Darlington, 15 Wall. 63, 21 L. Ed. 45, much relied upon in argument, was sufficiently distinguished from cases such as we have here in Hays v. Gauley Mountain Coal Co., 247 U. S. 189, 191, 62 L. Ed. 1061, 1062, 38 Sup. Ct. Rep. 470. The differences in the statutes involved render inapplicable the expressions in the opinion in that case (*not necessary to the decision of it*) as to distinctions between income and increase of capital.

In Lynch v. Turrish, 247 U. S. 221, 62 L. Ed. 1087, 38 Sup. Ct. Rep. 537, also much relied upon, it is expressly stated that, 'according to the fact admitted, there was no increase after that date (March 1, 1913), and therefore no increase subject to the law.' For this reason the questions here discussed and decided were not there presented." (65 L. Ed. 756.)

(b) *Shares of Stock are Movable Property within the meaning of Section 1390, Revised Laws of Hawaii 1925.*

The Supreme Court of Hawaii in its decision refers to Section 1390, which provides that in estimating gains, profits and income "there shall be included * * * the amount of sales of all movable property, less the amount expended in the purchase or production of same * * *." Appellant in his brief (page 43) argues that shares of stock do not come within the purview of that section because they should be considered as intangible property, and that the statute, in referring to movables, denotes only tangible property.

Section 3350, Revised Laws of Hawaii 1925 (Section 6729, R. L. 1935) provides:

“The shares of the several members in the stock of any incorporated company, whether owning real estate or otherwise, shall be deemed in law personal property.”

Shares of stock are, therefore, personal property by virtue of the above statute, and as the legislature has made no distinction between tangible and intangible property, we submit that the term “movable property” includes shares of stock.

In *Carter v. Hill*, 31 Haw. 264 (aff. 47 F. (2d) 869), the court treated securities, including shares of stock, and bank deposits as movable property within the meaning of Section 1390, although it held that the income therefrom was not taxable by the Territory where such property was held in New York by a resident of the Territory. The conclusion follows, therefore, that stocks and securities are considered as personal property (movable property) under the territorial tax laws.

Furthermore, it was held in *Castle v. Castle*, 267 F. 521, that under Section 2977, Revised Laws of Hawaii 1915, which provided that a married woman on the death of her husband was “entitled by way of dower to an absolute property in one-third part of all his *movable effects* in possession or reducible to possession at the time of his death,” a widow was entitled to one-third of the proceeds of her husband’s life insurance policies.

- (c) *The Court below Determined Appellant’s Liability for the Tax Assessed under Section 1388, Revised Laws of Hawaii 1925, and considered Section 1390 to show Legislative Intent.*

Frear v. Wilder, 25 Haw. 603, relied upon by the appellant (brief, page 43), held that Section 1307, Revised Laws of Hawaii 1915 (Section 1390, R. L. 1925) "merely prescribes the method to be pursued by the taxpayer in returning his gross income from which his net taxable income is to be computed," and that Section 1305, Revised Laws of Hawaii 1915 (Section 1388, R. L. 1925) "levies an income tax upon gains, profits and income derived from certain definite and plainly enumerated sources and fixes the rate of taxation."

The Supreme Court of Hawaii in its decision in the case at bar (Record, pages 35 to 36) stated that under Section 1388 "liability would accrue for taxes on income which was 'received' or 'derived' during the taxation period, which was the year 1930; * * *." The court then referred to Section 1390, which fixes the method to be followed by the taxpayer in returning his gross income. According to *Frear v. Wilder, supra*, Section 1390 is immaterial in so far as the question of tax liability is concerned, and it does not apply to "gains, profits and income" derived or received by the taxpayer during the taxation period, and that only Section 1388 does that.

The Supreme Court in the instant case determined the *liability* for the appellant's income tax under Section 1388, and then considered Section 1390 to show the legislative intent. It was not held that the tax liability was to be determined under the provisions of Section 1390 because after saying that: "The requirement of the statute was that in January, 1931, liability would accrue for taxes

on income which was 'received' or 'derived' during the taxation period, which was the year 1930;" the court went on to say, "this is made even more clear with *reference* to the sales of movable property * * *" as provided in Section 1390 (Record, page 35). Since the legislature had made no exception as to the time when such increment accrued, the court held that it could not make an exception.

Consequently, the distinction between these sections mentioned in *Frear v. Wilder, supra*, is not material.

The only question before the court in *Frear v. Wilder* was whether or not a Christmas gift to the taxpayer of shares of stock was taxable as income under the income tax laws. Income received as a result of the sale of "movable property" was not considered by the court, nor was the time when the income accrued to the taxpayer in issue.

7.

THAT THE TAX UPON THE INCOME OF THE APPELLANT FOR THE YEAR 1930 WAS CORRECTLY COMPUTED.

The appellant argues on page 46 "we may also mention one certain error in the computation of the tax. The tax is on income derived or received in 1930. But the evidence is that the payment of 40% of Lord's federal taxes—being \$20,328.50—was not made until 1931; (Ex. 29, Rec. p. 108, Ex. 30, Rec. p. 109, Rec. p. 118), hence clearly no tax for the year 1930 was payable on that amount on any theory."

This issue is raised for the first time before this court.

A complete answer to this argument is that the appellant returned in his tax return the entire amount received from E. J. Lord, Limited (Record, pages 1 to 7). Under "income" it appears that the appellant received from E. J. Lord, Limited, during the year 1930, \$408,457.98. He claimed that it was exempt income. Under schedule "B" he stated that he received \$60,000. This makes a total of \$468,457.98—the total amount paid to him by E. J. Lord, Limited, for his stock.

Section 1393, Revised Laws of Hawaii 1925, provides in part:

"Sec. 1393. Individual return. It shall be the duty of all persons of lawful age having an income of one thousand dollars (\$1,000.00) or more, for any taxation period, from all sources, and of all corporations made liable to income tax, to make and render a list or return between the first and thirty-first day of January of each year, in such form as the treasurer of the Territory may direct, to the assessor of the division in which such persons or corporations reside, locate or do business, of the amount of their or its income, gains and profits as aforesaid; * * *."

Pursuant to this statute the appellant filed his return which showed the amount received from E. J. Lord, Limited. The aggregate amount of \$468,457.98 included the amount of \$20,328.50. Having returned the amount as having been received in 1930, appellant is in no position to complain upon it being assessed and taxed. His return is an admission. If his income was not correctly computed (which we do not admit) his own conduct was the

cause of the error. He never requested to amend his return in this particular, or to be permitted to file any other or corrected return.

In addition it appears from the record that if any amounts were received in 1931 they were merely adjustments on amounts already paid (Record, page 118).

Furthermore, it is possible that appellant's books were kept upon an accrual basis. The amount accrued in 1930 under the agreement dated December 26, 1930 (Record, pages 90 to 93). It provided "and the party of the first part (E. E. Black, Limited) will pay forty per cent (40%) of the federal and territorial income tax which shall be assessed against the party of the second part by reason of and resulting from the sale and transfer by him of said shares of E. E. Black, Limited."

8.

THE APPELLANT HAS WAIVED ANY OBJECTION TO THE COMPUTATION OF THE TAX.

In addition to what has been stated under the last point, it affirmatively appears that after the appellant returned the amount of \$20,328.50 as having been received during the year 1930, he treated the same throughout the hearing before the Territorial Board of Equalization and later before the Supreme Court as being of the same character as the other amounts received from the sale of his stock.

Moreover, no claim was made to the Territorial Board of Equalization or the Supreme Court that the tax was erroneously computed in the respect mentioned. For that reason any objection was waived.

See: *Blair v. Oesterlain Machine Co.*, 72 L. Ed. 249, 275 U. S. 220;

Duignan v. United States, 71 L. Ed. 996, 274 U. S. 195.

9.

THE ASSIGNMENTS OF ERROR DO NOT
RAISE FOR REVIEW THE QUESTION AS
TO WHETHER THE TAX WAS CORRECTLY
COMPUTED.

There is no assignment of error covering or raising the question as to whether the tax and the amount of appellant's income for the taxable year 1930 were correctly computed.

We submit that appellant's contention comes within the well settled rule as set forth in *Cyclopedia of Federal Procedure*, Vol. 6, page 677, that:

"The court will restrict its consideration to questions and matters properly presented below and saved for review in some legal manner, and shown by the record."

This court stated in *Baldwin v. United States*, 72 F. (2d) 810, at page 812:

"This court has repeatedly held that errors argued in the briefs but not assigned as error will not be considered. *Holsman v. U. S.* (C.C.A. 9), 248 F. 193, 198; *Wight v. Washoe County Bank* (C.C.A.), 251 F. 819; *Pattis v. U. S.* (C.C.A.), 17 F. (2d) 562."

To the same effect Mr. Chief Justice White said:

"While it is not necessary, we deem it well to say, that in reviewing the action of the court below, we are, of course, confined to the record and the case therein made, and may not, as the result of mistaken suggestions as to the issues and proof, disregard our duty by deciding, not the case as made, but an imaginary one, wherein issues not made and not presented below would have to be supplied, and whereby conjecture and surmise must be indulged to replace the total absence of all proof on a particular subject."

Roura v. Government of the Philippine Islands,
218 U. S. 386, 54 L. Ed. 1080.

CONCLUSION

We respectfully submit that the decision and judgment of the Supreme Court of Hawaii should be affirmed.

Dated at Honolulu, T. H., this 1st day of May, 1935.

Respectfully submitted,

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